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ACCESSION NBR: 8612090729 DDC DATE: 86/12/05 NOTARIZED: NO DOCKET #
 FACIL: STN-50-529 Palo Verde Nuclear Station, Unit 2, Arizona Publi 05000529
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 RECIP. NAME RECIPIENT AFFILIATION
 MIRAGLIA, F. J. Division of Pressurized Water Reactor Licensing - B (post 8

SUBJECT: Forwards four vols of transaction documents re 860818
 closing of sale & leaseback transactions w/two equity
 investors & 861106 issuance of lease obligation bonds. Index
 attached to each vol.

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December 5, 1986

Director of Nuclear Reactor Regulation
Attention: Frank J. Miraglia, Director
Division of Pressurized Water Reactor
Licensing-B
Nuclear Regulatory Commission
Washington, D.C. 20555

Re: Sale and Leaseback Transactions by Arizona
Public Service Company--Palo Verde Nuclear
Generating Station Unit 2
(Docket No. STN 50-529)

Dear Mr. Miraglia:

Enclosed herewith on behalf of Arizona Public Service Company (APS) in connection with the above-captioned docket are two (2) volumes of transaction documents relating to (i) the August 18, 1986 closing of sale and leaseback transactions with two (2) equity investors (consummated, in part, with the proceeds of interim bank financing) and (ii) the November 6, 1986 issuance of \$273,000,000 of Lease Obligation Bonds, Series 1986, the proceeds of which were used to replace the interim bank financing with long-term public debt (the Public Offering). An index is attached to each volume indicating the documents contained therein.

Certain of the enclosed documents are amendments to other documents. In addition to amendments and supplements necessary to reflect the Public Offering, the transaction documents were amended in certain other respects in connection with the Public Offering. None

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*Boos Limited
1/1 Dist*

of the amendments is, however, deemed to be material to the previous action taken by the Commission and the staff of the Commission. Furthermore, none of the changes are changes that, had they been incorporated into the original transaction documents and not by amendment, would have altered, or caused APS to modify or condition, any of the representations and conditions material to the Commission's action on APS's Application in Respect of Sale and Leaseback Transactions dated May 2, 1986 and submissions supplemental thereto.

If I can be of further assistance, please do not hesitate to call at (212) 510-7750.

Sincerely,

Timothy Michael Toy
Timothy Michael Toy

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ARIZONA PUBLIC SERVICE COMPANY

Sale and Leaseback of an Undivided
Interest in Palo Verde Nuclear Generating
Station Unit 2

Emerson Capital Corporation

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PARTICIPATION AGREEMENT

dated as of August 1, 1986

among

EMERSON FINANCE CO.,
as Equity Participant

BANK OF AMERICA
NATIONAL TRUST AND SAVINGS ASSOCIATION,
for itself and as Agent for the Original Loan
Participants under the Bank Agency Agreement,
as Agent

PVNGS FUNDING CORP., INC.,
as Funding Corporation

THE FIRST NATIONAL BANK OF BOSTON,
in its individual capacity and as Owner Trustee
under a Trust Agreement,
dated as of August 1, 1986,
with Emerson Finance Co., as Owner Trustee

CHEMICAL BANK
in its individual capacity and as Indenture Trustee
under a Trust Indenture, Mortgage, Security Agreement
and Assignment of Facility Lease, dated as of
August 1, 1986,
with the Owner Trustee, as Indenture Trustee

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest
in Palo Verde Nuclear Generating Station Unit 2

Emerson Finance Co.

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PARTICIPATION AGREEMENT

THIS PARTICIPATION AGREEMENT, dated as of August 1, 1986, among EMERSON FINANCE CO., a Delaware corporation (the Equity Participant), BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, for itself (Bank of America) and as agent for the Original Loan Participants listed on Schedule 1 hereto (the Agent), PVNGS FUNDING CORP., INC., a Delaware corporation (the Funding Corp), THE FIRST NATIONAL BANK OF BOSTON, a national banking association, in its individual capacity (FNB) and as Owner Trustee (the Owner Trustee) under a Trust Agreement, dated as of August 1, 1986, with Emerson Finance Co., CHEMICAL BANK, a New York banking corporation, in its individual capacity (Chemical) and as Indenture Trustee (the Indenture Trustee) under a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, with the Owner Trustee, and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee or APS).

W I T N E S S E T H :

WHEREAS, the Equity Participant desires to cause the Trust to acquire the Undivided Interest and the Real Property Interest and to lease the Undivided Interest and the Real Property Interest to the Lessee under the Facility Lease;

WHEREAS, the Lessee desires to sell the Undivided Interest and the Real Property Interest to the Trust and lease the Undivided Interest and the Real Property Interest back from the Trust under the Facility Lease;

WHEREAS, in order to give effect to the foregoing sale and leaseback, the Owner Trustee and the Lessee are willing to enter into the Purchase Documents with respect to the sale and purchase of the Undivided Interest and the Real Property Interest;

WHEREAS, pursuant to the terms and provisions of the Indenture, the Owner Trustee will authorize the creation, issuance and sale and delivery of the Initial Series Notes and the granting of the security therefor, and the Indenture Trustee will authenticate the Initial Series Notes; and

WHEREAS, the Original Loan Participants are willing to purchase the Initial Series Notes on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For the purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A. References in this Participation Agreement to sections, paragraphs and clauses are to sections, paragraphs and clauses in this Participation Agreement unless otherwise indicated.

SECTION 2. Participation by the Original Loan Participants and Funding Corp; Releveraging; Refunding; Reoptimization.

(a) Original Loan Participants' Commitments; Direction to the Indenture Trustee. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), on the Closing Date each Original Loan Participant agrees to make a secured loan (a Loan) to the Owner Trustee, on a non-recourse basis, in an amount equal to such Original Loan Participant's Loan Percentage of the Facility Cost. The Agent, on behalf of the Original Loan Participants, as purchasers of the Initial Series Notes to be issued on the Closing Date, hereby (i) authorizes and directs the Indenture Trustee to execute, deliver and perform this Participation Agreement and (ii) authorizes and directs the Indenture Trustee to register each Initial Series Note issued on the Closing Date in the names provided to the Indenture Trustee hereunder and, upon authentication and delivery thereof pursuant to this Participation Agreement and the Indenture, to deliver such Initial Series Notes to the Agent. Each Loan Participant acknowledges and agrees, or by becoming a Holder of a Refunding Note will be deemed to have acknowledged and agreed, that, in connection with this Participation Agreement, the Indenture Trustee shall have the benefits and protections of Article VIII of the Indenture and that, in the event of a conflict between the provisions of this Participation Agreement and the Indenture, the Indenture Trustee shall, as between the Indenture Trustee and the Loan

Participants, be fully protected in relying on the express terms of the Indenture.

(b) Failure to Fund. In the event any Original Loan Participant shall fail to make any amount of its Loan available to the Agent pursuant to subsection (c) below, no other Original Loan Participant shall have any obligation to increase any amount of its Loan. In the event the Equity Participant shall fail to make any amount of its Investment available on the Closing Date pursuant to Section 3, the Original Loan Participants shall have no obligation to make any amount of their Loans available on such Date, or to increase any amount of any of their Loans.

(c) Funding of Loans; Fees; Terms of Initial Series Notes.

(i) Not later than the close of business on the Business Day immediately prior to the Closing Date, the Agent shall make available to Chemical funds in an amount equal to the maximum aggregate amount of the Loans specified by Lessee in its Notice of Closing pursuant to Section 5(a), and Chemical shall hold such funds in the Agent's name in a Trust Investment Account (the Investment Account). Chemical shall invest such funds at the direction of the Lessee, with the reasonable consent of the Agent, and earnings on such Investment Account shall be for the account of the Lessee. Subject to the terms and conditions of this Participation Agreement and upon satisfaction of the conditions precedent in Sections 5(a) and 11(a), the Agent shall, on the Closing Date, transfer title to the Investment Account in an amount equal to the actual aggregate amount of the Loans specified by the Lessee in its certificate pursuant to Section 11(a)(2) to the Indenture Trustee for the account of the Owner Trustee.

(ii) On the Closing Date, the Owner Trustee shall pay to the Agent, for the benefit of each Original Loan Participant, a fee equal to one-eighth of one percent ($1/8$ of 1%) of such Original Loan Participant's committed amount set forth on Schedule 1 hereto.

(iii) On the Closing Date, the Lessee shall pay to the Agent an Arrangement Fee as described in that certain letter agreement dated June 27, 1986, between the Lessee and Bank of America.

(iv) The Loans shall be evidenced by one or more Initial Series Notes. The Initial Series Notes shall be issued by the Owner Trustee as registered Notes under and pursuant to the Indenture and shall, in the aggregate, be in the principal amount of the respective Loans, bear interest at the rate or rates per annum and be payable as set forth in the Indenture and the Initial Series Notes.

(d) Request for Refinancing. Subject to Sections 2(e) and 11(c), the Lessee may request by written notice to the Equity Participant, the Loan Participant or Participants, the Owner Trustee and the Indenture Trustee that the Equity Participant arrange for a non-recourse loan (a Refunding Loan) to the Owner Trustee, the proceeds of which shall be used to prepay the aggregate principal amount of Outstanding Notes on the Refunding Date and the expenses incurred in connection therewith. In addition, if any Refunding Loan is to be made following any event referred to in Section 3(d) of the Facility Lease, the Lessee may request, subject to Sections 2(e) and 11(c), that the Equity Participant arrange for an additional simultaneous loan (a Releveraging Loan) to the Owner Trustee in an amount which shall minimize the Basic Rent payments by the Lessee over the Basic Lease Term while preserving the Equity Participant's Net Economic Return. Subject to the satisfaction of the provisions of this paragraph (d), and further subject to its ability to raise funds, Funding Corp, upon the request of the Lessee, agrees to lend to the Owner Trustee the amount of the applicable Refunding Loan and any simultaneous Releveraging Loan. In connection with any Refunding Loan, the Lessee may request the Equity Participant to arrange an adjustment to the amounts of principal scheduled to be paid in respect of Outstanding Notes on each Basic Rent Payment Date so as to minimize the Basic Rent payments by the Lessee over the Basic Lease Term while preserving the Equity Participant's Net Economic Return.

(e) Procedures Applicable to and Limitations on Refunding Loans and any Releveraging Loans. Each of the Lessee, the Owner Trustee, the Equity Participant and each Loan Participant agrees that it will cooperate in connection with any Refunding Loan or Releveraging Loan and enter into such additional agreements and such supplements or amendments to or consents under each of the Transaction Documents as may reasonably be requested by the Lessee to effectuate the transactions contemplated in connection with such Refunding Loan and any simultaneous Releveraging Loan; provided, however, that the Lessee may not request more than three Refunding Loans and two Releveraging Loans; and provided, further, that (a) prior to June 30, 1989, the Lessee may request only one Refunding Loan which is not in the form of long-term, fixed-rate non-recourse indebtedness of the Owner Trustee and (b) on and after June 30, 1989, the Lessee may request only one Refunding Loan. Notwithstanding the foregoing, the Equity Participant need not participate in any Refunding Loan or Releveraging Loan or reoptimization (i) which is not in compliance with Revenue Procedure 75-21 and 75-28 (or any similar regulations or procedures), (ii) which would result in the Facility Lease being treated differently for accounting purposes than it was treated immediately prior to such Refunding Loan or Releveraging Loan or reoptimization or (iii) the maturity date of which would extend beyond the scheduled date for the termination of the Basic Lease Term. Proceeds of any Refunding Loan and simultaneous Releveraging Loan shall be paid directly to the Indenture Trustee in immediately available funds at the Indenture Trustee's Office and applied (x) to the extent necessary, to refund the unpaid principal amount of the Outstanding Notes and to pay expenses in connection therewith, and (y) to the extent of the Releveraging Loan, as a partial refund of the Investment. Each Refunding Loan and simultaneous Releveraging Loan shall be aggregated and evidenced by Refunding Notes (the Refunding Notes), in the respective principal amounts requested by the Lessee, each of which Notes shall be issued by the Owner Trustee under and pursuant to the Indenture, be in the respective principal amounts indicated in the foregoing request, bear interest at the respective rates per annum and be payable, in each case as set forth in, or determinable under, the Indenture. The Lessee shall give the parties hereto at least (i) 30 days prior written notice of a proposed Refunding Date and (ii) five Business Days' prior written notice of an actual Refunding Date. Not

less than three Business Days prior to the Refunding Date, the Loan Participant or Participants shall deliver to the Equity Participant and the Lessee a certificate setting forth the information necessary to complete the Refunding Notes (including the respective schedules thereto). Upon such delivery, and upon approval by the Lessee and the Equity Participant of the terms thereof, the Equity Participant and the Lessee shall cause the respective forms of Refunding Notes to be completed. The parties hereto shall cooperate in the preparation and execution of such amendments to the Transaction Documents as shall be necessary or appropriate to effect such refunding; provided, however, that such amendments shall not, in the opinion of independent tax counsel selected by the Equity Participant, adversely affect the tax benefits contemplated by the Equity Participant in entering into the transactions contemplated by this Participation Agreement and the other Transaction Documents.

(f) Reoptimization. Subject to the satisfaction of the conditions set forth in Sections 2(e) and 11(c), if the Lessee, in a timely manner, provides the Owner Trustee and the Equity Participant with information sufficient for the Owner Trustee to direct the adjustments described in Section 3.12 of the Indenture, together with a certificate (in form and substance reasonably satisfactory to the Equity Participant) to the effect that such adjustments minimize the aggregate increase in Basic Rent occurring as a result of the operation of Section 3(d) of the Facility Lease, while preserving Net Economic Return, the Owner Trustee shall deliver to the Indenture Trustee a certificate pursuant to such Section 3.12 of the Indenture. Notwithstanding the foregoing, the Equity Participant and the Owner Trustee may rely on such certificate of the Lessee and shall have no obligation to verify the same.

SECTION 3. Participation by the Equity Participant; Partial Refund of the Investment.

(a) Equity Participant's Commitment. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), on the Closing Date the Equity Participant agrees to provide funds to the Trust as follows: (i) an amount (such amount, as it may be reduced from time to time in accordance with Section 3(b), being herein called the Investment) equal to the Investment Percentage of the Facility Cost for the purpose of

acquiring the Undivided Interest and the Real Property Interest and (ii) an amount equal to Closing Date Transaction Expenses. Proceeds of the Investment shall be made available to the Indenture Trustee, in immediately available funds, at the Indenture Trustee's Office in such manner as the Lessee and the Equity Participant shall agree. Closing Date Transaction Expenses shall be paid to the Owner Trustee, in immediately available funds, at 100 Federal Street, Boston, Massachusetts 02110, Attention: Manager, Corporate Trust Department.

(b) Partial Refund. In the event that the Indenture Trustee shall have received the proceeds of any Releveraging Loan, the Indenture Trustee shall, immediately upon its receipt thereof, disburse the same to the Owner Trustee for disposition in accordance with the Trust Agreement as a partial refund of the Investment, and for purposes hereof the Investment shall thereupon be reduced accordingly.

SECTION 4. Purchase, Sale, Financing and Lease of the Undivided Interest and the Real Property Interest.

(a) The Undivided Interest. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), receipt from the Equity Participant of the Investment and receipt from the Agent of the proceeds of the Loans made by the Original Loan Participants, the Owner Trustee shall (i) on the Closing Date cause the Trust to purchase the Undivided Interest from the Lessee for the amount specified in the Notice of Closing as the "Purchase Price" (the Purchase Price), and (ii) promptly after receipt of the amount thereof from the Equity Participant, disburse the Closing Date Transaction Expenses, in each case in accordance with the payment instructions in the Notice of Closing. Subject to the satisfaction of the conditions in Section 11(b), on the Closing Date the Lessee shall sell the Undivided Interest to the Trust for the Purchase Price. Concurrently with such purchase and sale, the Trust shall lease the Undivided Interest to the Lessee, and the Lessee shall lease the Undivided Interest from the Trust, pursuant to the Facility Lease.

(b) The Real Property Interest. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a) and receipt from the Equity Participant of the Investment, on the Closing Date the Equity Participant shall cause the Trust to acquire the Real Property Interest from the Lessee for a purchase price equal to the amount set forth in Schedule 2 as the "Real Estate Investment". Subject to the satisfaction of the conditions in Section 11(b), on the Closing Date the Lessee shall sell the Real Property Interest to the Trust for the amount set forth in Schedule 2 as the Real Estate Investment. Concurrently with such purchase and sale, the Trust shall lease the Real Property Interest to the Lessee, and the Lessee shall lease the Real Property Interest from the Trust, pursuant to the Facility Lease.

SECTION 5. Notice of Closing; Closing.

(a) Notice of Closing. Not later than 10:00 a.m., New York time, two Business Days prior to the Closing Date, the Lessee shall deliver to the Equity Participant, the Owner Trustee, the Agent and the Indenture Trustee a notice, substantially in the form of Schedule 2 (the Notice of Closing), which shall (i) state that the Closing Date shall occur on the date specified therein, (ii) list the then known Transaction Expenses payable by the Owner Trustee pursuant to Section 14(a) (the Closing Date Transaction Expenses), (iii) provide payment instructions in respect of the disposition of the Purchase Price, the Real Estate Investment and Closing Date Transaction Expenses and (iv) specify the maximum aggregate amount of the Loans.

(b) Closing. Upon satisfaction or waiver of the conditions in Sections 5(a) and 11(a) and receipt from the Equity Participant of the Investment and the amount of Closing Date Transaction Expenses and from the Agent of the proceeds of the Loans, on the Closing Date the Owner Trustee shall cause the Purchase Price to be paid and the purchase price of the Real Property Interest to be paid and shall disburse Closing Date Transaction Expenses, in each case in funds immediately available on the Closing Date and in accordance with the payment instructions in the Notice of Closing. Upon satisfaction of the conditions in Section 11(b), on or as of the Closing Date the Lessee shall deliver to the Owner Trustee the Purchase Documents.

SECTION 6. Representations, Warranties and Agreements of Funding Corp.

(a) Representations and Warranties. Funding Corp represents and warrants that:

(1) **Due Organization.** Funding Corp is a corporation duly organized and validly existing in good standing under the laws of the State of Delaware and has the corporate power and authority to carry on its business as presently conducted, own its properties, and enter into and perform its obligations under this Participation Agreement.

(2) **Due Authorization.** This Participation Agreement has been duly authorized by all necessary corporate action on the part of Funding Corp and does not require the consent or approval of its stockholder or any trustee or holder of any of its indebtedness or other obligations.

(3) **Execution and Enforceability.** This Participation Agreement has been duly executed and delivered by Funding Corp and constitutes its legal, valid and binding agreement, enforceable against it in accordance with its terms.

(4) **No Violation.** Neither the execution, delivery or performance by Funding Corp of this Participation Agreement, nor the consummation by Funding Corp of the transactions contemplated hereby, nor compliance by Funding Corp with the provisions hereof, conflicts with, or results in the breach of any provision of, or is inconsistent with, the Certificate of Incorporation or By-Laws of Funding Corp or contravenes any Federal, Delaware or New York law applicable to it, or any indenture, mortgage or agreement to which Funding Corp is a party or by which it or its property is bound, or requires any Governmental Action with respect to Funding Corp on or before the Closing Date under any Federal, Delaware or New York law applicable to it.

(5) **No Other Business.** Except as contemplated by this Participation Agreement, the other Transaction Documents and any Financing Documents and except as otherwise contemplated by the Section 6(c) Application, Funding Corp has not

engaged in any business or activity of any type or kind whatever.

(6) ERISA. Funding Corp will not acquire any Refunding Note with the "plan assets" of any "employee benefit plan", within the meaning of Section 3(3) of ERISA, or any "plan", within the meaning of Section 4975(e)(1) of the Code.

(7) Investment Representation. Funding Corp will acquire each Refunding Note to be acquired by it hereunder and under the Indenture solely for purposes of pledging such Refunding Note to the Collateral Trust Trustee to secure Bonds issued from time to time under the Collateral Trust Indenture. Funding Corp understands that no Refunding Note to be acquired by it hereunder or under the Indenture will have been registered under the Securities Act and that each such Refunding Note will bear the legend set forth in Section 4.5 of the Indenture.

(b) Agreements. Funding Corp agrees that:

(1) Transfers of Notes. Any transfer or assignment of any Note acquired by it or of all or any part of Funding Corp's interest hereunder or under any other Transaction Document or any Financing Document shall be effected in a transaction constituting an exempted transaction under the Securities Act and on the express condition that the transferee, assignee or participant shall agree to be bound by the terms and provisions hereof and thereof. Neither Funding Corp nor any subsequent Holder of a Note may sell, exchange or transfer any Note to any other Person (other than the Collateral Trust Trustee) unless such transferee delivers to the Lessee, the Equity Participant, the Owner Trustee and the Indenture Trustee a representation and warranty (and an opinion of counsel satisfactory to each such Person) to the effect that neither the transfer of such Note to, nor the ownership of such Note by, such transferee will cause such transferee, or any such Persons, to be engaged in a "prohibited transaction", as defined in section 406 of ERISA or section 4975 of the Code, which is not at such time subject to an exemption contained in ERISA or in the rules, regulations, releases or bulletins adopted thereunder.

(2) Prepayment of Bonds. Except as provided in this Participation Agreement, Funding Corp will not refinance or optionally prepay any Bond issued in connection with any Refunding Note without the consent of the Equity Participant and the Lessee.

(3) Quiet Enjoyment. Funding Corp acknowledges Section 6(a) of the Facility Lease.

(4) No Other Business. During such time as any Note acquired by Funding Corp is outstanding and held by the Collateral Trust Trustee as security for obligations of Funding Corp, Funding Corp will not (i) engage in any business or activity other than (1) in connection with the Transaction Documents or (2) as otherwise contemplated by the Section 6(c) Application or (ii) amend or engage in any activity or take any action not permitted by Article THIRD, FOURTH or SIXTH of its Certificate of Incorporation, as in effect on the date of execution and delivery hereof, without, in each case, the consent of the Lessee, the Equity Participant, the Owner Trustee and the Indenture Trustee.

(c) Agreements With the Indenture Trustee. Funding Corp hereby (i) acknowledges and agrees that, in connection with this Participation Agreement, the Indenture Trustee shall have the benefits and protections of Article VIII of the Indenture and (ii) agrees that, to the extent it becomes a Loan Participant, in the event of a conflict between the provisions of this Participation Agreement and the Indenture, the Indenture Trustee shall, as between the Indenture Trustee and Funding Corp, be fully protected in relying on the express terms of the Indenture.

SECTION 7. Representations, Warranties and Agreements of the Equity Participant.

(a) Representations and Warranties. The Equity Participant represents and warrants that:

(1) Due Organization. The Equity Participant is a corporation duly organized and validly existing in good standing under the laws of the State of Delaware and has the corporate power and authority to enter into and perform its obligations under this Participation Agreement and each other Transaction Document to which it is a party.

(2) Due Authorization. This Participation Agreement and each other Transaction Document to which the Equity Participant is a party have been duly authorized by all necessary corporate action on the part of the Equity Participant and do not require the consent or approval of its stockholder or any trustee or holder of any of its indebtedness or other obligations, except such as have been duly obtained, given or accomplished.

(3) Execution and Enforceability. This Participation Agreement and each other Transaction Document to which the Equity Participant is a party have been duly executed and delivered by the Equity Participant and constitute its legal, valid and binding agreement, enforceable against it in accordance with its terms.

(4) No Violation. Neither the execution, delivery or performance by the Equity Participant of this Participation Agreement or any other Transaction Document to which it is a party, nor the consummation by the Equity Participant of the transactions contemplated hereby or thereby, nor compliance by the Equity Participant with the provisions hereof or thereof, conflicts with, or results in the breach of any provision of, or is inconsistent with, its documents of incorporation or By-Laws or contravenes any Applicable Law applicable to it, or any indenture, mortgage or agreement for borrowed money to which the Equity Participant is a party or any other agreement or instrument to which the Equity Participant is a party or by which it or its property is bound or requires any Governmental Action with respect to the Equity Participant under Federal, New York, Delaware or Connecticut law applicable on or before the Closing Date, except such as are contemplated by the Transaction Documents or such as have been duly obtained, given or accomplished; provided, however, that the Equity Participant makes no representation or warranty as to any Applicable Law or Governmental Action relating to the Securities Act (other than as expressly set forth in clause (8) of this Section 7(a)), the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear

matters, public utilities, the environment, health and safety or Unit 2.

(5) No Equity Participant's Liens. Neither the execution and delivery by the Equity Participant of this Participation Agreement or any other Transaction Document to which the Equity Participant is, or is to become, a party, nor the performance by the Equity Participant of its obligations hereunder or thereunder, will subject the Trust Estate or the Lease Indenture Estate, or any portion of either thereof, to any Equity Participant's Lien.

(6) Acquisition for Investment. The Equity Participant is acquiring the beneficial interest in the Trust and the Trust Estate for its own account, for investment and not with a view to, or for sale in connection with, any distribution thereof in violation of Section 5 of the Securities Act; provided, however, that nothing herein shall prohibit a disposition of the Equity Participant's property in compliance with all Applicable Law.

(7) No Prior Security Interest. There exists no security interest in or other Lien on the Lease Indenture Estate in the States of Arizona, Delaware or Connecticut arising as a result of claims against the Equity Participant unrelated to the transactions contemplated by the Transaction Documents which is prior to the Indenture Trustee's security interest in and Lien on the Lease Indenture Estate.

(8) Securities Act. The Equity Participant has not directly or indirectly offered or sold, or authorized anyone to directly or indirectly offer or sell, any security issued or to be issued to finance Unit 2, or any security the offering of which for the purposes of the Securities Act would be deemed to be part of the offerings contemplated by the Transaction Documents, or solicited any offer to acquire any such security from any Person, in violation of Section 5 of the Securities Act.

(9) ERISA. The Equity Participant is not acquiring its interest in the Trust with the "plan assets" of any "employee benefit plan" within the meaning of section 3(3) of ERISA or any "plan" within the meaning of section 4975(e)(1) of the Code.

(10) Location of the Chief Executive Office. The chief executive office of the Equity Participant for purposes of Article 9 of the UCC is at 111 East Prospect, Stamford, CT 06904, Attention: President.

(b) Agreements. The Equity Participant agrees and, to the extent set forth in Section 7(b)(4), the Lessee also agrees that:

(1) No Equity Participant's Liens. The Equity Participant will not create or permit to exist, and, at its own cost and expense, will promptly take such action as may be necessary duly to discharge, all Equity Participant's Liens.

(2) Quiet Enjoyment. The Equity Participant acknowledges the provisions of Section 6(a) of the Facility Lease and Section 8(c) of this Participation Agreement.

(3) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, the Equity Participant will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of, or in respect of, Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(4) Transfer of Interest in the Trust Estate. If the Lessee shall not have assumed the Notes as contemplated by Section 3.9(b) of the Indenture and the Lessor shall not have Transferred the Undivided Interest to the Lessee in accordance with Section 9(c), 9(d) or 16(e) of the Facility Lease, then, upon receipt by the Equity Participant, from the Indenture Trustee or otherwise, of the payments specified in Sections 9(c), 9(d) or 16(e) of the Facility Lease, the Equity Participant shall assign, convey and transfer (the Special Transfer) to the Lessee all of the Equity Participant's right, title and interest in, to and under the Trust Estate (except Excepted Rights and the right to receive Excepted Payments), such transfer to be effected by the execution and delivery by the Equity Participant of a Bill of Sale and Assignment substantially in

the form of Appendix B hereto but without any further act' (whether under any Transaction Document or otherwise) by the Owner Trustee, the Equity Participant, any Loan Participant, the Lessee, the Indenture Trustee or any other Person, whereupon the Lessee shall be deemed for all purposes to have assumed, and the Equity Participant shall be deemed for all purposes to have been released from, all obligations and liabilities of the Equity Participant under this Participation Agreement and the other Transaction Documents (other than in respect of obligations under Sections 7(b)(1), (2) and (3) of this Participation Agreement incurred prior to the effectuation of the Special Transfer which shall survive, and shall continue in effect following, the Special Transfer). At any time following the occurrence of an Event of Loss or a Deemed Loss Event, or at any time when an Event of Default shall have occurred and be continuing, the Equity Participant may effect the Special Transfer, whether or not the Equity Participant shall have received the payments referred to in the preceding sentence or the payments specified in Section 16(a) of the Facility Lease, as the case may be, whereupon (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding, and (ii) the Facility Lease shall become a security agreement for all purposes of Applicable Law.

If at the time of the Special Transfer the Equity Participant shall not have received the payments specified in the first sentence of the preceding paragraph or the payments specified in Section 16(a) of the Facility Lease, as the case may be, the obligation of the Lessee to make such payments (together with interest thereon at the Penalty Rate) shall continue until so received, and such obligation shall be secured by (and the Lessee hereby grants to the Equity Participant a security interest in and general lien upon) all the Lessee's right, title and interest in, to and under the Trust Estate. In connection therewith, the Lessee hereby agrees that (i) the Equity Participant shall have all the rights and remedies of a secured party under the UCC, (ii) the Lessee hereby appoints the Equity

Participant as its attorney-in-fact, irrevocably, with full power of substitution, to ask, require, demand, receive and give acquittance for any and all moneys and claims for moneys due and to become due to the Lessee under or arising out of the Trust Estate, to endorse any checks or other instruments or orders in connection therewith, and to take any action (including the filing of financing statements or other documents and the delivery of written instructions to the Owner Trustee and the Indenture Trustee specifying that all payments to be made to the Lessee under the Trust Agreement and the Indenture shall be made directly to the Equity Participant) or institute any proceedings which the Equity Participant may deem necessary or appropriate to protect and preserve such security interest and the rights of the Equity Participant to receive payments thereunder, (iii) until all amounts due to the Equity Participant have been received by the Equity Participant, the Lessee (in its capacity as such and as transferee under the Special Transfer) shall not, without the prior written consent of the Equity Participant, take any action or deliver any instruction under, or accept or approve any amendment to, any Transaction Document the effect of which would be to (A) relieve or otherwise affect the obligation of the Lessee to make such payments, (B) terminate the Trust Agreement, (C) terminate or rescind the Facility Lease or (D) sell, assign, transfer or deliver the Trust Estate to any Person and (iv) the Lessee agrees, from time to time, to do all such acts and execute all such instruments of further assurance as shall be reasonably requested from time to time by the Equity Participant for the purpose of fully carrying out and effectuating this Section 7(b)(4) and the intent hereof.

On the date which is 100 days after the receipt by the Equity Participant of all amounts due to the Equity Participant, the security interest and lien hereinabove provided shall, so long as the Lessee is not then the subject of any bankruptcy, insolvency or similar proceeding, terminate, and the Equity Participant, at the request of the Lessee, shall execute and deliver to the Lessee such termination statements, releases or other instruments presented to the Equity Participant as shall be reasonably required to effect such termination.

Following an Event of Loss, a Deemed Loss Event or the exercise of the Cure Option, the Lessee shall promptly commence and diligently pursue best efforts to (i) satisfy all of the conditions set forth in Section 3.9(b) of the Indenture and (ii) assume the obligations represented by the Initial Series Notes, notwithstanding any intervening Special Transfer.

The Lessee warrants to and for the benefit of the Holders of Notes that a Special Transfer effected in accordance with the provisions of this Section 7(b)(4) will not invalidate, impair, interrupt or otherwise restrict the Lessee's obligation to pay Rent in accordance with the terms of the Facility Lease or the Lessor's rights and remedies with respect to such obligation. The Lessee covenants that it will designate an Affiliate as transferee in connection with a Special Transfer if such designation is necessary to prevent a breach of the warranty in the foregoing sentence. The Lessee agrees that (i) it will provide to the Indenture Trustee an opinion of counsel, in form and substance satisfactory to the Indenture Trustee, to the effect that the Special Transfer did not, at the time thereof (or, if delivered prior to the Special Transfer, will not), invalidate, impair, interrupt or otherwise restrict the Lessee's obligation to pay Rent in accordance with the terms of the Facility Lease, (ii) the opinion of counsel described in subclause (i) of this sentence will, if practicable in the Lessee's judgment, be delivered to the Indenture Trustee prior to the Special Transfer, but in no event before the date on which the event giving rise to the Special Transfer occurred or more than 30 days after the date of the Special Transfer, and (iii) if the opinion of counsel described in subclause (i) of this sentence is not delivered in accordance with subclause (ii) of this sentence, such non-delivery shall be deemed to be and shall conclusively establish that the Lessee breached the warranty contained in the first sentence of this paragraph. Anything to the contrary notwithstanding, nothing herein shall be construed or interpreted to mean or imply that the Equity Participant or the Lessee cannot effect a Special Transfer on the terms and in the manner described herein or that a breach of the Lessee's warranty in the first sentence of this paragraph shall affect in any way

the Equity Participant's entitlement to payment in accordance with this Section 7(b)(4).

SECTION 8. Representations, Warranties and Agreements of the Owner Trustee and FNB.

(a) Representations and Warranties. FNB as Owner Trustee and (except as otherwise provided in the last sentence of this Section 8(a)) in its individual capacity, represents and warrants that:

(1) Due Organization. FNB is a national banking association duly organized and validly existing in good standing under the laws of the United States of America and has all requisite corporate power and authority to enter into and perform its obligations under (x) the Trust Agreement and, to the extent it is a party hereto in its individual capacity, this Participation Agreement and (y) acting as Owner Trustee, this Participation Agreement and each other Transaction Document to which FNB is a party as Owner Trustee.

(2) Due Authorization; Enforceability; etc. This Participation Agreement and each other Transaction Document to which FNB is a party have been duly authorized by all necessary corporate action of FNB (in its individual capacity or as Owner Trustee, as the case may be) and, upon execution and delivery hereof and thereof, this Participation Agreement and each such other Transaction Document will have been duly executed and delivered and will be a legal, valid and binding agreement of FNB (in its respective capacities), enforceable against it (in its respective capacities) in accordance with its terms; it being understood that FNB is not making any representation or warranty as to the priorities of the Liens created or to be created under any Transaction Document, title to the Trust Estate or recordings or filings necessary in connection therewith.

(3) Notes. Upon execution of each Note to be issued by the Owner Trustee under the Indenture pursuant hereto, authentication thereof by the Indenture Trustee pursuant to the Indenture and delivery thereof against payment therefor in accordance with this Participation Agreement, such Note will be a legal, valid and binding obligation

of the Owner Trustee, enforceable against the Owner Trustee in accordance with its terms.

(4) No Violation. Neither the execution and delivery by (x) FNB of the Trust Agreement and, to the extent FNB is a party hereto in its individual capacity, this Participation Agreement and (y) the Owner Trustee of this Participation Agreement and each other Transaction Document (other than the Trust Agreement) to which the Owner Trustee is a party, nor the performance by FNB, in its individual capacity or as Owner Trustee, as the case may be, of its obligations under each thereof, conflicts with, or results in the breach of any provision of, its Articles of Association or By-Laws and does not contravene any Applicable Law of the United States of America or The Commonwealth of Massachusetts governing the banking or trust powers of FNB, and does not contravene any provision of, or constitute a default under, any indenture, mortgage, contract or other instrument to which FNB is a party or by which it is bound or require any Governmental Action with respect to the Owner Trustee under any Federal or Massachusetts law, except such as are contemplated by the Transaction Documents or such as have been duly obtained, given or accomplished; provided, however, that no representation or warranty is made with respect to (i) the right, power or authority of FNB or the Owner Trustee to act under the ANPP Participation Agreement or the License in respect of the Undivided Interest or Unit 2, (ii) as to any Applicable Law or Governmental Action relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Nuclear Waste Act, the Federal Power Act, the Atomic Energy Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 or (iii) the Trust Estate or the Lease Indenture Estate to the extent either may constitute real property under Applicable Law.

(5) Defaults. To the best knowledge of the Owner Trustee, no Indenture Default or Indenture Event of Default has occurred and is continuing. The Owner Trustee is not in violation of any of the terms of this Participation Agreement or any other Transaction Document to which it is a party.

(6) Litigation: There is no action, suit, investigation or proceeding pending or, to the knowledge of FNB, threatened against FNB (in any capacity) before any court, arbitrator or administrative or governmental body and which relates to its banking or trust powers which, individually or in the aggregate, if decided adversely to the interests of FNB in such capacity, would have an adverse effect upon the ability of FNB (in any capacity) to perform its obligations under this Participation Agreement or any other Transaction Document to which it (in any capacity) is a party.

(7) Location of the Chief Place of Business and Chief Executive Office, etc. The chief place of business and chief executive office of the Owner Trustee and the office where its records concerning the accounts or contract rights relating to the transactions contemplated hereby are kept are located in Boston, Massachusetts.

(8) No Prior Security Interest. There exists no security interest in the Lease Indenture Estate in the State of New York or Arizona or in The Commonwealth of Massachusetts arising as a result of any claim against FNB unrelated to the transactions contemplated by the Transaction Documents or the Financing Documents which is prior to the Indenture Trustee's security interest in the Lease Indenture Estate.

(9) No Lessor's Liens. Neither the execution by FNB (in any capacity) of this Participation Agreement or any other Transaction Document to which it (in any capacity) is a party, nor the performance in such capacity by it of its obligations hereunder or thereunder, will subject the Trust Estate or the Lease Indenture Estate, or any portion thereof, to any Lessor's Lien.

The representations and warranties in Section 8(a)(2) and Section 8(a)(3), as to Transaction Documents and each Note being legal, valid and binding obligations enforceable in accordance with their respective terms, are given only by FNB in its capacity as Owner Trustee and not in its individual capacity, except that FNB does represent in its individual capacity that it is authorized under the laws of The Commonwealth of

Massachusetts to execute and deliver the Transaction Documents to which it is a party.

(b) Agreements. FNB agrees, in its individual capacity, that:

(1) Discharge of Liens. FNB will not create or permit to exist, and will, at its own cost and expense, promptly take such action as may be necessary duly to discharge, all Lessor's Liens.

(2) Certain Amendments. Unless a Default or an Event of Default has occurred and is continuing or an Event of Loss or Deemed Loss Event has occurred, FNB will not amend any of the payment terms of any Note or take any action to refund any Note after the date of issue thereof pursuant to the terms of this Participation Agreement and the Indenture without the prior written consent of the Lessee. Except for amendments or supplements made pursuant to Article X of the Trust Agreement or contemplated by Section 7(b)(4), FNB will not amend or supplement, or consent to any amendment of or supplement to, the Trust Agreement without the prior written consent of the Lessee unless a Default or an Event of Default has occurred and is continuing or the Lease Termination Date has occurred or an Event of Loss or Deemed Loss Event has occurred, if such amendment would materially and adversely affect the rights of the Lessee under the Facility Lease or this Participation Agreement.

(3) Change in Location of Chief Place of Business and Chief Executive Office, etc. FNB shall notify the Lessee, the Loan Participant, the Equity Participant, Funding Corp and the Indenture Trustee promptly after any change in the location of its chief executive office, principal and chief place of business or place where its records concerning the accounts or contract rights relating to the transactions contemplated hereby are kept.

(4) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, FNB (in any capacity) agrees that it will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in

respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(5) Quiet Enjoyment. FNB acknowledges Section 6(a) of the Facility Lease.

(c) Agreements. The Owner Trustee agrees that:

(1) Rights in Relation to ANPP Participants. The rights and remedies of the Owner Trustee and the Equity Participant in the Undivided Interest and in the Real Property Interest are subject and subordinate to the rights and remedies of the ANPP Participants (other than (i) the Lessee or (ii) any Person who shall become an ANPP Participant in respect of the Lessor's Interest) under the ANPP Project Agreements.

(2) Lessee to be an ANPP Participant. Except as provided in Sections 15.2.2, 15.6.4 and 15.10 (or any comparable successor provisions) of the ANPP Participation Agreement, the Lessee shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Lessor and the Indenture Trustee) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of the Lessee transferred to the Lessor pursuant to the Transaction Documents; provided, however, that the foregoing shall not limit in any way any liability or obligation that the Lessee may incur to the Owner Trustee or the Equity Participant under any Transaction Document as a result thereof.

(3) Cash Bids. On the Lease Termination Date and upon the Lessee failing to purchase or otherwise reacquire all the right, title and interest in PVNGS and contractual rights related thereto necessary for the operation of the interest (the Lessor's Interest) acquired by the Lessor pursuant to the Transaction Documents, the Lessor shall, and, subject to the rights of the Lessee to renew for the Renewal Term or purchase the Undivided Interest and the Real Property Interest pursuant to the Facility Lease, at any time prior to the Lease Termination

Date the Lessor may, entertain cash bids from each ANPP Participant for the Lessor's Interest.

(4) Survival. The provisions of Sections 8(c)(1), (2) and (3) shall remain in full force and effect until such time as the ANPP Administrative Committee or the ANPP Participants shall otherwise consent, by amendment to the ANPP Participation Agreement or otherwise.

(5) License Matters. The Owner Trustee acknowledges that before taking possession of the Undivided Interest or the Real Property Interest or any part thereof or of any other interest in PVNGS, either of the following may be required: (i) the issuance of an appropriate license from the NRC, whether by amendment to the License or otherwise, or (ii) a partial transfer of the License authorizing the Lessor to possess its interest in PVNGS, to the extent of the Undivided Interest, upon application for partial transfer of the License to such extent filed pursuant to Applicable Law.

SECTION 9. Representations, Warranties and Agreements of Chemical.

(a) Representations and Warranties. Chemical represents and warrants that:

(1) Due Organization. Chemical is a banking corporation duly organized and validly existing in good standing under the laws of the State of New York and has the corporate power and authority and legal right to enter into and perform its obligations under the Indenture, this Participation Agreement and each other Transaction Document to which it is a party.

(2) Due Authorization; Enforceability, etc. This Participation Agreement and each other Transaction Document to which Chemical is a party have been duly authorized by all necessary corporate action on the part of Chemical and each has been duly executed and delivered by Chemical.

(3) Authentication of Each Note. The officer of Chemical who shall authenticate any Note to be issued pursuant to the Indenture shall be, at the time of such authentication, an Authorized Officer.

(4) No Violation. Neither the execution and delivery by Chemical of this Participation Agreement or the Indenture, nor the authentication by it of the Notes, nor the consummation by it of the transactions contemplated hereby or thereby, nor the compliance by it with the provisions hereof or thereof will contravene any Applicable Law governing its banking or trust powers, or contravene or result in a breach of, or constitute a default under, its Articles of Incorporation or By-laws, or require any Governmental Action under any Federal or New York or Arizona law, except such as have been, or on or before the Closing Date will have been, duly obtained, given or accomplished; provided, however, that no representation or warranty is made as to (i) any Applicable Law or Governmental Action relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Nuclear Waste Act, the Federal Power Act, the Atomic Energy Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 or (ii) the Lease Indenture Estate to the extent it may constitute real property under Applicable Law.

(b) Agreements. The Indenture Trustee agrees that:

(1) Agreement to Discharge Liens. The Indenture Trustee will not create or permit to exist, and will promptly take such action as may be necessary duly to discharge, all Indenture Trustee's Liens.

(2) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, the Indenture Trustee agrees that it will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(3) Quiet Enjoyment. The Indenture Trustee acknowledges Section 6(a) of the Facility Lease.

SECTION 10. Representations, Warranties and Agreements of the Lessee.

(a) Representations and Warranties. The Lessee represents and warrants that:

(1) **Due Organization.** APS is a corporation duly organized and validly existing in good standing under the laws of the State of Arizona and has the corporate power and authority to carry on its business as presently conducted, to own or hold under lease its properties and to enter into and perform its obligations under this Participation Agreement and each other Transaction Document to which it is a party. APS is duly qualified and in good standing to do business as a foreign corporation in the State of New Mexico and has not failed to qualify to do business or to be in good standing in any other jurisdiction where failure so to qualify or be in good standing would materially and adversely affect the financial condition of APS or its ability to perform any obligations under this Participation Agreement or any other Transaction Document to which it is a party. All of the issued and outstanding common stock of APS is owned by AZP Group, Inc.

(2) **Due Authorization.** The execution, delivery and performance by APS of this Participation Agreement and each other Transaction Document to which it is a party have been duly authorized by all necessary corporate action on the part of APS and do not, and will not, require the consent or approval of AZP Group, Inc. or any trustee or holder of any indebtedness or other obligation of APS, other than (i) the Mortgage Release, (ii) the finding of the ANPP Administrative Committee described in Section 15.6.2 of the ANPP Participation Agreement and (iii) such other consents and approvals as have been, or on or before the Closing Date, in the case of the Transaction Documents, or on or before any Refunding Date, in the case of any Refunding Loan, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant.

(3) **Execution.** This Participation Agreement and each other Transaction Document to which the Lessee is a party have been duly executed and delivered by APS, and this Participation Agreement

and each such Transaction Document constitute the legal, valid and binding agreements of APS, enforceable against it in accordance with their respective terms.

(4) No Violation, etc. Neither the execution, delivery or performance by the Lessee of this Participation Agreement or any other Transaction Document to which it is a party, nor the consummation by the Lessee of the transactions contemplated hereby or thereby, nor compliance by the Lessee with the provisions hereof or thereof, conflicts or will conflict with, or results or will result in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or By-Laws of APS or any Affiliate of APS, or any Applicable Law, or any indenture, mortgage, lease or any other agreement or instrument to which APS or any Affiliate of APS is a party or by which the property of APS or any Affiliate of APS is bound, or results or will result in the creation or imposition of any Lien (other than Permitted Liens) upon any property of APS or any Affiliate of APS. There is no provision of the Restated Articles of Incorporation or By-Laws of APS, or any Applicable Law, or any such indenture, mortgage, lease or other agreement or instrument which materially adversely affects, or in the future is likely (so far as the Lessee can now foresee) to materially adversely affect, the business, operations, affairs, condition, properties or assets of the Lessee, or its ability to perform its obligations under this Participation Agreement or any other Transaction Document to which it is a party.

(5) Governmental Actions. No Governmental Action under any Federal (including, without limitation, the Federal Power Act), Arizona or New York law is or will be required in connection with the execution, delivery or performance by the Lessee of, or the consummation by the Lessee of the transactions contemplated by, this Participation Agreement or any other Transaction Document to which it is a party, except such Governmental Actions (i) as have been, or on or before the Closing Date, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant, (ii) as may be required under existing Federal, Arizona or New York

law to be obtained, given or accomplished From time to time after the Closing Date in connection with the maintenance, use, possession or operation of Unit 2 or otherwise with respect to Unit 2 and the Lessee's or the Operating Agent's involvement therewith and which are, for PVNGS, routine in nature and which the Lessee has no reason to believe will not be timely obtained, (iii) as may be required under Applicable Law not now in effect and (iv) as may be required in connection with any Refunding Loan (which will have been duly obtained, given or accomplished by the Refunding Date). No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required (a) in connection with the participation by the Owner Trustee, the Indenture Trustee, Funding Corp., the Equity Participant, or any Loan Participant in the consummation of the transactions contemplated by this Participation Agreement, any other Transaction Document or any Financing Document or (b) to be obtained by any of such Persons during the Lease Term, except such Governmental Actions (i) as have been, or on or before the Closing Date, in the case of the Transaction Documents, or any Refunding Date, in the case of any Refunding Loan or any Financing Documents, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of any obligations issued under and pursuant to the Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required by existing Applicable Law if, after the Lease Termination Date,

the Lessee should redeliver the Undivided Interest to the Lessor pursuant to Section 5(a) of the Facility Lease or provide transmission services for the Owner Trustee and sell an undivided interest in the Retained Assets to the Lessor as provided under the Assignment and Assumption, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person in connection with taking possession of its interest in Unit 2. Nothing in the License or the License Amendment or any other Governmental Action with respect to the NRC will materially interfere with the ability of the Owner Trustee to transfer or convey the Undivided Interest and the Real Property Interest to a person, partnership, corporation or governmental corporation or agency engaged in the generation, transmission or distribution of energy who will be in a position to enjoy all the benefits of, have all the rights of, and be an ANPP Participant, so long as such person, partnership, corporation or governmental corporation or agency complies with the licensing requirements of the NRC and obtains, or becomes a transferee of, a license from the NRC.

(6) Securities Act. Neither APS nor anyone acting on its behalf has directly or indirectly offered or sold any Bond, any interest in any Note, any note issued with respect to any other undivided interest in Unit 2, the Undivided Interest or any other undivided interest in Unit 2, the Facility Lease or any other lease of an undivided interest in Unit 2, or any similar security or lease, or any interest in any security or lease the offering of which, for purposes of the Securities Act, would be deemed to be part of the same offering as the offering of the aforementioned securities or leases, or solicited any offer to acquire any of the aforementioned securities or leases, in each case in a manner which would constitute a violation of Section 5 of the Securities Act, and except as contemplated by this Participation Agreement, neither the Lessee nor any one authorized to act on its behalf will take any action which would subject the issuance or sale of any Note or any interest in the Facility Lease or any other debt instrument (other than the Bonds) issued or to be issued to finance the Undivided Interest to the registration requirements of such Section 5.

(7) Title to the Undivided Interest; Real Property Interest; Security Interest. On the Closing Date, (i) good and marketable title to the Undivided Interest will be duly, validly and effectively conveyed and transferred to the Owner Trustee, free and clear of all Liens other than the Liens indicated on the title report delivered pursuant to Section 11(a)(30) and other Liens relating to obligations not in excess of \$15,000,000, (ii) good and marketable title to the Real Property Interest will be duly, validly and effectively created in the Owner Trustee, as provided in the Deed, (iii) APS will have good and marketable title to its ownership interest in the Retained Assets, free and clear of all Liens except Permitted Liens, the lien of the Existing Mortgage and matters disclosed in the title report referred to in Section 11(a)(30), (iv) the Lessee will have good and valid title to its ownership interest in the PVNGS Site, (v) Unit 2 will be wholly located on the PVNGS Site without any material encroachments by any portion thereof on any other property, (vi) all filings and recordings necessary or advisable to perfect the Owner Trustee's right, title and interest in and to the Undivided Interest and the Real Property Interest, and to perfect for the benefit of the Indenture Trustee and the holders of the Notes, the security interest, mortgage and assignment of facility lease provided for in the Indenture, will in each case have been duly made and (vii) no other action, including any action under any fraudulent conveyance statute, will be required to protect the title and interests of the Owner Trustee in and to the Undivided Interest and Real Property Interest, in each case against the claims of all Persons other than the ANPP Participants under the ANPP Project Agreements, or to perfect such security interest, mortgage and assignment of facility lease in favor of the Indenture Trustee.

(8) Non-Interference. None of the Permitted Liens described in clauses (ii), (iii), (iv), (v), (vii), (viii) and (xii) of the definition of such term will, on and after the Closing Date, materially interfere with the use or possession of the Undivided Interest or the Real Property Interest or the use of or the exercise by the Owner Trustee of its rights under the Purchase Documents and the Assignment and Assumption with respect to the

interests in PVNGS granted or to be granted under the Purchase Documents and the Assignment and Assumption. Nothing in the ANPP Participation Agreement or in any ANPP Project Agreement will materially interfere with the ability of the Owner Trustee to transfer or convey the Undivided Interest and the Real Property Interest to a person, partnership, corporation or governmental corporation or agency engaged in the generation, transmission or distribution of energy, who will be in a position to enjoy all the benefits of, have all the rights of, and be an ANPP Participant.

(9) Personal Property. Unit 2, based on the agreements of the Lessee and the other ANPP Participants in the ANPP Participation Agreement and of the Lessee and the Owner Trustee herein and in the other Transaction Documents, is to the full extent permitted by Applicable Law personal property.

(10) Location of Chief Executive Office. The chief executive office and place of business of the Lessee and the office where it keeps its records concerning its accounts or contract rights is located at 411 North Central Avenue, Phoenix, Arizona 85004.

(11) Financial Statements. The consolidated balance sheets of APS (A) as of December 31, 1985 and 1984, respectively, and the related consolidated statements of income, retained earnings and changes in financial position for each of the years in the three-year period ended December 31, 1985, together with the notes accompanying such financial statements, all certified by Deloitte Haskins & Sells, and (B) as of June 30, 1986 and 1985, respectively, and the related consolidated statements of income, retained earnings and changes in financial position for the six-month periods ended June 30, 1986 and June 30, 1985, respectively, all certified by the Treasurer or an Assistant Treasurer of APS, as furnished to the Equity Participant and the Original Loan Participants, fairly present the consolidated financial position of APS at each such date and the results of its operations for each of the periods then ended, in conformity with generally accepted accounting principles applied on a consistent basis, subject in the case of the consolidated balance

sheets and the related consolidated statements described in clause (B) above, to the condensation of certain financial information and the omission of certain footnote disclosures as permitted by the rules and regulations of the SEC and to year-end audit adjustments. The Lessee knows of no such adjustments which would, if made on the date hereof, be material.

(12) Disclosure. None of the financial statements to which reference is made in paragraph 11 above, nor the reports to which reference is made in this paragraph 12, nor any certificate, written statement or other document prepared by or for, or at the direction of, the Lessee and furnished to the Equity Participant by the Lessee in connection with the transactions contemplated hereby (under the circumstances, at the time and for the purposes for which any statement made therein was made) contains any untrue statement of a material fact or omits to state a material fact necessary to make the statements therein not misleading. There is no fact known to the Lessee that materially and adversely affects or, so far as the Lessee can now reasonably foresee, is likely to materially and adversely affect, the business or financial condition of APS or any material portion of its properties or the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document or Financing Document to which the Lessee is, or is to become, a party except as disclosed in APS's Annual Report on Form 10-K for the year ended December 31, 1985, APS's Quarterly Reports on Form 10-Q for the quarters ended March 31, 1986 and June 30, 1986, respectively, and APS's Current Reports on Form 8-K filed on January 22, 1986 and June 19, 1986, copies of which have been provided to the Equity Participant.

(13) Litigation. There is no action, suit, investigation or proceeding pending or, to the knowledge of the Lessee, threatened against APS before any court, arbitrator or administrative or governmental body which questions the validity or enforceability of this Participation Agreement or any other Transaction Document and, except as disclosed in the reports to which reference is made in paragraph 12, there is no action, suit, investigation or proceeding pending or, to the best

knowledge of the Lessee, threatened against APS before any court, arbitrator or administrative or governmental body which, individually or in the aggregate, if decided adversely to the interests of the Lessee, would have a material adverse effect on the business or financial condition of APS or materially and adversely affect the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document or Financing Document to which it is, or is to become, a party.

(14) Tax Returns. The Lessee has filed all Federal, state, local and foreign, if any, tax returns which were required to be filed, and has paid all Taxes shown to be due and payable on such returns and has paid all other Taxes in respect of the Lessee's interest in Unit 2 and in the PVNGS Site which are payable by the Lessee to the extent the same have become due and payable and before they have become delinquent, except for (i) any Taxes the amount, applicability or validity of which may be in dispute and which are currently being contested in good faith by appropriate proceedings and with respect to which APS has set aside on its books reserves (segregated to the extent required by generally accepted accounting principles) deemed by it to be adequate and (ii) any Taxes relating to PVNGS in respect of which the Operating Agent has not given notice to APS that the same are due and payable. The Federal income tax returns of APS have been audited by the IRS for taxable years through December 31, 1982.

(15) ERISA. In reliance upon, and subject to the accuracy of, the representations made by the Equity Participant in Section 7(a)(9), the execution and delivery of this Participation Agreement and the other Transaction Documents to which the Lessee is a party will not involve any prohibited transaction within the meaning of ERISA or section 4975 of the Code.

(16) Regulation. So long as the Facility Lease is in effect, assuming the proper filing of Form U-7D with the SEC on or within 30 days after the Closing Date, under Applicable Law now in effect, neither any Loan Participant, the Equity Participant, FNB nor the Owner Trustee will be or

become, solely by reason of either its entering into this Participation Agreement or any other Transaction Document to which any of them is, or is to become on or before the Closing Date, a party, or the transactions contemplated hereby or thereby, subject to regulation (i) as an electric utility, a public utility or a holding company by any Federal or Arizona public utility commission or other regulatory body, authority or group (including, without limitation, the SEC, the FERC or the Arizona Corporation Commission) or (ii) in any manner by the NRC.

(17) Authorizations, etc. The Lessee has not failed to obtain any Governmental Action under any Federal or Arizona law or other authorization, license, approval, permit, consent, right or interest under any Federal or Arizona law, where a failure to obtain such would materially and adversely affect the ability of APS to carry on its business as presently conducted.

(18) No Default, etc. APS is not in default, and no condition exists that, with the giving of notice or lapse of time or both, would constitute a default by APS, under the Existing Mortgage or any other material mortgage, deed of trust, indenture, lease, contract or other instrument or agreement to which APS is a party or by which it or any of its properties or assets may be bound.

(19) Certain Documents. True and correct copies of the ANPP Participation Agreement, the Material Project Agreements and the Existing Mortgage have been delivered to counsel to the Equity Participant. No ANPP Project Agreement will, on and after the Closing Date, materially and adversely interfere with (i) except (in the case of the Generation Entitlement Share only) for the ANPP Participation Agreement, the title of the Owner Trustee to the Undivided Interest or the Real Property Interest, or (ii) except for the ANPP Participation Agreement, the use of, or the exercise by the Owner Trustee of its rights under the Facility Lease, the Real Property Interest, the Purchase Documents and the Assignment and Assumption with respect to, the Undivided Interest and the interests in the PVNGS Site (including the Real Property Interest) granted or to be granted under

the Purchase Documents and the Assignment and Assumption. No payment default or other default of a material nature by the Lessee has occurred and is continuing under the Existing Mortgage or any ANPP Project Agreement. Each of the ANPP Participation Agreement and the other ANPP Project Agreements is in full force and effect and no breach of any thereof, to the Lessee's knowledge, by any other party thereto has occurred and is continuing, except where the failure to be in force and effect or such breach would not have a material and adverse effect on the Undivided Interest (including the related Generation Entitlement Share), the Real Property Interest, Unit 2 or the rights, interest and benefits of the Owner Trustee or the Equity Participant under any Transaction Document. Upon execution and delivery of the Mortgage Release and the recordation thereof or of UCC releases in respect thereof, (i) the mortgagee and secured party thereunder will have released the lien of the Existing Mortgage on the Undivided Interest and (ii) the rights of the Owner Trustee in the Undivided Interest and the Real Property Interest will not be and will not become subject or subordinate to the rights of any Person, except the Indenture Trustee under the Indenture and the ANPP Participants under, and to the extent expressly set forth in, the ANPP Participation Agreement (as in effect on the Closing Date) and except as may otherwise expressly be permitted by the Facility Lease. The lien of the Existing Mortgage does not extend to rights of the Lessee under any Transaction Document (other than the Lessee's leasehold interest under the Facility Lease).

(20) Unit 2. The description of Unit 2 set forth in Exhibit B to the Bill of Sale, as delivered on the Closing Date, will be correct and sufficiently complete to identify such property.

(21) Investment Company Act. The Lessee (a) is not an "investment company", or a company "controlled" by an "investment company", within the meaning of the Investment Company Act and (b) is a "subsidiary company" of a "holding company", AZP Group, Inc., and an "affiliate" of a "holding company", as such terms are defined in the Holding Company Act, but is exempt from all provisions of the Holding Company Act and the rules thereunder

(except Section 9(a)(2) of the Holding Company Act).

(22) Sale and Conveyance. The sale and conveyance of the Undivided Interest, the Real Property Interest and any other property or interest in property transferred by APS under the Transaction Documents will not render APS insolvent nor is it being made in contemplation of APS's insolvency; the property remaining in the hands of APS after such sale, conveyance and transfer is not an unreasonably small capital; APS does not intend to or believe that it will incur debts beyond its ability to pay as they mature; and APS has no actual intent to hinder, delay or defraud either present or future creditors.

(b) Agreements.

(1) Delivery of Documents. The Lessee shall deliver to the Equity Participant and the Loan Participant (and, in the case of Sections 10(b)(1)(iii) and 10(b)(1)(iv), the Owner Trustee):

(i) Financial Statements: (A) as soon as practicable, and in any event within 120 days, after the end of each fiscal year of the Lessee, a consolidated balance sheet of the Lessee as of the end of such fiscal year and related consolidated statements of income, retained earnings and changes in financial position for such year, all in reasonable detail and certified in an opinion by a nationally recognized firm of independent public accountants, and the annual and interim reports of the Lessee to holders of its securities as soon as the same have been mailed to such holders, (B) as soon as practicable, and in any event within 60 days, after the end of each fiscal quarter (other than the last fiscal quarter) of each fiscal year of the Lessee, a consolidated balance sheet of the Lessee as of the end of said period and a related consolidated statement of income, retained earnings and changes in financial position for said period, all in reasonable detail, and certified by the Chief Financial Officer, the Controller or an Assistant

Controller, the Treasurer or an Assistant Treasurer of the Lessee and (C) as soon as practicable and in any event within 15 days of their being filed with the SEC, copies of all documents filed by the Lessee with the SEC pursuant to the reporting requirements of the Securities Exchange Act;

(ii) Other Reports: promptly upon their becoming available, any registration statement, offering statement, investment memorandum or prospectus prepared by the Lessee in connection with the public offering of securities (other than public offerings of securities under employee stock option, consumer stock or dividend reinvestment plans);

(iii) Notice of Default: promptly upon the Lessee becoming aware of the existence thereof, written notice specifying any condition which constitutes a Default, an Event of Default, an Indenture Default or an Indenture Event of Default or a default by any ANPP Participant under the ANPP Participation Agreement and, in each case, the nature and status thereof;

(iv) Annual Certificate: within 120 days after the end of each fiscal year of the Lessee, a certificate of the Lessee, signed by the Chief Financial Officer, the Controller, an Assistant Controller, the Treasurer or an Assistant Treasurer of the Lessee, to the effect that such officer has reviewed, or caused to be reviewed by individuals under his supervision, this Participation Agreement and each other Transaction Document and each Financing Document to which the Lessee is a party, and has made, or caused to be made under his supervision, a review of the transactions contemplated hereby and thereby and the condition of the Lessee and its subsidiaries during such preceding fiscal year, and such review has not disclosed the existence during such fiscal period, nor does such officer have knowledge of the existence as at the date of such certificate, of any condition or event that constitutes a Default or Event of Default or, if any such condition or event

exists, specifying the nature and period of existence thereof and any action the Lessee has taken, is taking, or proposes to take with respect thereto;

(v) Opinion of Counsel: within 120 days after the end of each fiscal year of the Lessee, an opinion or opinions, satisfactory to the Equity Participant, the Owner Trustee, the Collateral Trust Trustee and the Indenture Trustee, of Snell & Wilmer, counsel for the Lessee, and/or other counsel acceptable to the Equity Participant (A) either to the effect that (1) all filings and recordations (or refilings and rerecordations) required to (i) convey to the Owner Trustee, and preserve the title of the Owner Trustee to, the Undivided Interest and the Real Property Interest, and (ii) so long as any Note is Outstanding, grant, perfect, and preserve the security interest of the Indenture Trustee in the Lease Indenture Estate have been duly made, or (2) no such additional filings, recordings, refilings or rerecordings are necessary, and (B) specifying the particulars of all action required during the period from the date of such opinion through the last day of the next succeeding calendar year, including, in the case of each UCC continuation statement required to be filed during such period, the office in which each such continuation statement is to be filed and the filing date and filing number of the original financing statement or fixture filing to be continued, and the dates within which such continuation statement may be filed under Applicable Law;

(vi) ANPP Information: upon receipt by the Lessee, unless prohibited by Applicable Law and subject to applicable confidentiality undertakings with respect thereto, copies of (A) minutes of all committee meetings of the ANPP Administrative Committee, the ANPP Engineering and Operating Committee, the ANPP Auditing Committee and other committees composed of the ANPP Participants, (B) all annual capital budgets, annual operation and maintenance budgets and monthly statistical reports on the operation of PVNGS, (C) all

notices to or from the NRC with respect to violations or other material occurrences with respect to PVNGS, and (D) Institute of Nuclear Power Operations evaluation reports;

(vii) Requested Information: with reasonable promptness, unless prohibited by Applicable Law, such other data and information as to the business and properties of the Lessee or as to Unit 2, PVNGS or the PVNGS Site as from time to time may be reasonably requested by the Equity Participant, subject, however, to applicable confidentiality undertakings with respect thereto.

(2) Further Assurances. The Lessee shall cause to be promptly and duly taken, executed, acknowledged and delivered all such further acts, documents and assurances as any Loan Participant, the Owner Trustee or the Equity Participant may from time to time reasonably request in order to carry out more effectively the intent and purposes of this Participation Agreement, the other Transaction Documents and any Financing Documents, and the transactions contemplated hereby and thereby. The Lessee shall cause the financing statements (and continuation statements with respect thereto) and the documents enumerated and described in Schedule 5, and all other documents necessary or advisable in that connection, to be recorded or filed at such places and times, and in such manner, and will take all such other actions or cause such actions to be taken, as may be necessary or reasonably requested by any Loan Participant, the Equity Participant, the Collateral Trust Trustee, the Owner Trustee or the Indenture Trustee, in order to establish, preserve, protect and perfect the title of the Owner Trustee to the Undivided Interest and the Real Property Interest and the Owner Trustee's rights and interests under this Participation Agreement and the other Transaction Documents and, so long as any Note is Outstanding, the first and prior security interest of the Indenture Trustee in the Lease Indenture Estate.

(3) Covenants.

(i) Maintenance of Corporate Existence, etc. The Lessee shall at all times maintain

its existence as a corporation under the laws of the State of Arizona, except as permitted by paragraph (ii) below (including any consent given by the Equity Participant pursuant to such paragraph (ii)), and qualify and remain qualified to do business in each jurisdiction where the conduct of its business or the ownership of its properties requires such qualification. The Lessee will do or cause to be done all things necessary to preserve and keep in full force and effect its material franchises; provided, however, that the Lessee may discontinue or permit the discontinuance of any material franchise if (x) its board of directors shall determine that such discontinuance is necessary or desirable in the conduct of its business and does not materially and adversely affect or diminish any right of the Equity Participant or any Loan Participant or (y) the Lessee continues to provide electric service to the area covered by such material franchise to the substantially same extent and on substantially the same terms and conditions as provided prior to such discontinuance pending the renegotiation or renewal thereof.

(ii) Merger, Sale, etc. Without the consent of the Equity Participant, each Loan Participant and the Indenture Trustee, the Lessee shall not (1) consolidate with any Person, (2) merge with or into any Person, or (3) convey or transfer to any Person more than 10% of its total assets, including cash (determined, in each case, on the basis of the values of such assets, as shown on the most recent certified balance sheet of the Lessee delivered to the Equity Participant pursuant to Section 10(b)(1)(i)(A)), in any single transaction or series of related transactions, unless, immediately after giving effect to such transaction:

(A) the Person who is the Lessee under the Facility Lease immediately following such consolidation, merger, conveyance or transfer (the Surviving Lessee) shall be a corporation which (i) is organized under the laws of the United

States of America, a state thereof or the District of Columbia, (ii) is a utility which is a principal supplier of electric service to residents of Phoenix, Arizona, (iii) is an ANPP Participant under the ANPP Participation Agreement with respect to Unit 2 (including the Undivided Interest), (iv) shall have assumed each covenant and condition of the Lessee under the ANPP Participation Agreement and each other ANPP Project Agreement, and (v) holds a valid and subsisting license from the NRC to possess Unit 2 (including the Undivided Interest);

(B) the Surviving Lessee, if other than the Lessee immediately prior to such transaction, shall execute and deliver to the Equity Participant and the Indenture Trustee an agreement, in form and substance reasonably satisfactory to the Equity Participant, containing the assumption by the Surviving Lessee of each covenant and condition of this Participation Agreement and each other Transaction Document to which the Lessee immediately prior to such transaction was a party immediately preceding such transaction;

(C) no Default (other than a failure to deliver documents and other information specified in Section 10(b)(1)(vi)), Event of Loss or Deemed Loss Event shall have occurred and no Event of Default shall have occurred and be continuing;

(D) for the benefit of the Equity Participant only, the Surviving Lessee, if other than the Lessee immediately prior to such transaction, shall have provided a Letter of Credit which meets the requirements set forth in Section 10(b)(3)(ix) to the Equity Participant in the same amount as was available immediately prior to such transaction;

(E) the Surviving Lessee shall have delivered to the Equity Participant and

the Indenture Trustee an Officers' Certificate and an opinion, reasonably satisfactory to the Equity Participant, of independent counsel to the Surviving Lessee, each stating that (1) such transaction complies with this paragraph (ii) and (2) all conditions precedent to the consummation of such transaction have been satisfied and any Governmental Action required in connection with such transaction has been obtained, given or accomplished;

(F) the Surviving Lessee shall have delivered to the Equity Participant an opinion, reasonably satisfactory to the Equity Participant, of independent counsel to the Surviving Lessee, stating that such transaction does not and will not cause a Tax Loss (as defined in the Tax Indemnification Agreement);

(G) such transaction is otherwise permitted by and is in compliance with the ANPP Participation Agreement;

(H) (i) the Surviving Lessee shall have a debt to equity ratio of not more than 3 to 1 or (ii) the long-term unsecured debt securities of the Surviving Lessee shall be rated at least "investment grade", as determined by Moody's and Standard & Poors, if the Lessee has long-term unsecured debt securities rated by such rating organizations, or as determined by one of such rating organizations, if the Surviving Lessee has long-term unsecured debt securities rated by only one such organization, or, if neither of such rating organizations shall rate such debt securities of the Surviving Lessee at the time, by any nationally recognized rating organization in the United States of America; and

(I) the Surviving Lessee shall have a Net Worth not less than \$1,400,000,000.

Upon the consummation of such transaction the Surviving Lessee, if other than the Lessee, shall succeed to, and be substituted for, and may exercise every right and power of, the Lessee immediately prior to such transaction under this Participation Agreement and each other Transaction Document and Financing Document to which the Lessee immediately prior to such transaction was a party immediately prior to such transaction, with the same effect as if the Surviving Lessee had been named herein and therein.

(iii) Change in Chief Executive Office. The Lessee shall notify the Owner Trustee, the Equity Participant, each Loan Participant and the Indenture Trustee promptly after any change in the location of its chief executive office and place of business, principal place of business or place where the Lessee maintains its business records.

(iv) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of any Collateral Trust Indenture, the Lessee shall not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(v) ANPP Project Agreements. Except where the failure to do so would not have a material and adverse effect on the Undivided Interest, the Real Property Interest, Unit 2 or the rights, interests and benefits of the Owner Trustee, the Equity Participant or any Loan Participant under any Transaction Document, the Lessee at all times, unless the Equity Participant shall otherwise consent, shall (1) perform its obligations under and comply with the terms of each ANPP Project Agreement to be complied with by it, (2) exercise its rights under the ANPP Participation Agreement to maintain each ANPP Project Agreement in full force and effect, (3) keep

unimpaired all of the Lessee's rights, powers and remedies under each ANPP Project Agreement and prevent any forfeiture or impairment thereof, (4) take such action as may be available to it to cause the enforcement of the ANPP Participation Agreement in accordance with its terms, (5) not take or fail to take or join in any action with respect to or accept or approve (A) any amendment to or any other change in, the ANPP Participation Agreement or any other ANPP Project Agreement, or (B) any other action or change, the effect of which would be to relieve the Lessee of any obligations under the ANPP Participation Agreement on or after the Closing Date and (6) not accept or approve any amendment to any ANPP Project Agreement the effect of which would be to (A) reduce the Generation Entitlement Share included in the Undivided Interest, (B) relieve the Lessee of any obligation under the ANPP Participation Agreement in respect of the Undivided Interest or the Real Property Interest on or after the Closing Date, (C) impose, directly or indirectly, on the Owner Trustee or the Equity Participant at any time any obligations, (D) discriminate against (x) the Owner Trustee or the Equity Participant in its capacity as lessor in a sale and leaseback transaction or (y) any present or future ANPP Participant because such ANPP Participant derived or will derive its status as "Participant" under the ANPP Participation Agreement from a lessor in a sale and leaseback transaction, or (E) deprive the Owner Trustee or the Equity Participant, as the case may be, of the benefit of Sections 15.2.2, 15.10 and 32.1 of the ANPP Participation Agreement (or any comparable successor provisions). The Lessee shall (X) provide copies of any proposed amendment to or modification of the ANPP Participation Agreement to the Equity Participant not less than 45 days prior to the execution thereof by the Lessee (except where the Lessee is unaware thereof 45 days prior to such execution, in which case the Lessee shall provide notice thereof as promptly as possible after becoming so aware) and (Y) upon such execution furnish to the Equity Participant and the Indenture

Trustee a copy of any such amendment or modification as executed.

(vi) Notes and Bonds. The Lessee will not, and will not permit any of its Affiliates to, acquire any of the Notes or the Bonds.

(vii) Cooperation. The Lessee shall accept and cooperate in receiving the Special Transfer, either on its own behalf or, if the Equity Participant so requires, on behalf of the Person designated by the Lessee to receive the Special Transfer. If at the time a Special Transfer is effected, the Lessee shall not have assumed all obligations under the Initial Series Notes, the provisions of Section 4(a) (and related definitional provisions) of the form of Bank Exchange Note shall at all times thereafter be incorporated herein by reference (except that "Company" shall be "Lessee") until all Initial Series Notes are paid in full.

(viii) Decommissioning. (A) Unit 2, the Common Facilities used in respect of Unit 2, the other property included in the Unit 2 Retained Assets and allocable to Unit 2 and the portion of the PVNGS Site allocable to Unit 2 shall be decommissioned and retired from commercial service in accordance with Applicable Law and, to the extent a method of decommissioning is not prescribed by Applicable Law, by the method for decommissioning determined as provided in the ANPP Participation Agreement (the foregoing being herein referred to as Decommissioning). (B) As between the Lessee, the Owner Trustee, the Equity Participant, each Loan Participant and any transferee (including by way of lease) or assignee of any of the Lessor's or the Equity Participant's right, title or interest in Unit 2, the Lessee agrees to pay, be solely responsible for, and to indemnify such parties against, all costs and expenses relating or allocable to, or incurred in connection with, Decommissioning to the extent of a 29.1% undivided interest in Unit 2 (all such costs and expenses being herein referred to as Decommissioning Cost), notwithstanding (i) the

occurrence of the Lease Termination Date, any Default, Event of Default, Event of Loss, Deemed Loss Event or any other event or occurrence, (ii) any provision of any Transaction Document, or other document, instrument or agreement, including the ANPP Participation Agreement, (iii) any provision of the License or any other license or permit, or (iv) any Applicable Law, either now or hereafter in effect, charter or by-law provision, Governmental Action or other impediment, including, without limitation, the bankruptcy or insolvency of the Lessee; it being understood that the obligations of the Lessee under this clause (B) are and shall be absolute and unconditional. (C) The Lessee shall use its best efforts to cause the ANPP Administrative Committee to use the safest and most reliable method of Decommissioning consistent with public health and safety. (D) The Lessee shall establish a special decommissioning trust fund or funds (the Decommissioning Trust Fund) for the accumulation and full funding of amounts sufficient by December 31, 2015 to pay Decommissioning Cost. For this purpose, Decommissioning Cost shall be as determined by an expert selected by the Equity Participant and reasonably acceptable to the Lessee (the Decommissioning Expert). For purposes of making such determination, such expert shall assume that the method of Decommissioning Unit 2 shall be the costlier of (i) the DECON method of decommissioning (if not prohibited by Applicable Law), plus cost of removal, or (ii) the method of decommissioning required under Applicable Law. The Decommissioning Trust Fund shall be created as promptly as practicable after the Closing Date by the execution and delivery of the Decommissioning Trust Agreement. The Decommissioning Trust Fund shall be funded by the making of semi-annual deposits in the Decommissioning Trust Fund (with the first such semi-annual deposit to be made on or before the fifth anniversary of the Closing Date) by the Lessee in such amounts as would, based on investments in such securities as are permitted under the Decommissioning Trust Agreement and utilizing the actuarial

assumptions used by the Lessee as of the Closing Date for its pension fund, as such assumptions may be changed from time to time by the Lessee with the consent of the Equity Participant, result in the Decommissioning Trust Fund being funded by December 31, 2015 in the full amount of the Decommissioning Cost; provided, however, that such actuarial assumptions shall reflect that earnings on amounts deposited in the Decommissioning Trust Fund shall be subject to Federal income taxation until such time that under Applicable Law such earnings on such amounts will not be subject to Federal income taxation. During the first 25 years after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert every five years. Commencing in the 26th year after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert each year. Immediately following each such determination by the Decommissioning Expert prior to December 31, 2015, the Lessee will make appropriate adjustments, if required, in its semi-annual deposits to be made thereafter so that, based on the investment and actuarial assumptions then in effect with respect to the Decommissioning Trust Fund, such Fund will be funded in the full amount of the Decommissioning Cost as so determined by December 31, 2015. During the first 20 years following the Closing Date, the Decommissioning Trust Fund will be invested and reinvested in accordance with standards no more liberal than the investment guidelines and actuarial assumptions set forth in the Decommissioning Trust Agreement. Commencing in the 21st year following the Closing Date and thereafter, the Decommissioning Trust Fund will be invested and reinvested in Decommissioning Fund Permitted Investments; provided, however, that in no event shall the Decommissioning Trust Fund be invested in any securities of the Lessee or any Affiliate thereof. The Decommissioning Trust Fund shall be the fund of the Lessee, provided that the Lessor shall be granted and shall have a security interest in such fund as security for the obligations of the Lessee under this

Section 10(b)(3)(viii). If, after the Decommissioning of Unit 2, there shall be any funds remaining in the Decommissioning Trust Fund, such funds shall be the property of, and be paid to, the Lessee. (E) In the event that (i) the Facility Lease shall have expired or terminated on or after December 31, 2015, (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default) and (ii) thereafter the Lessor shall (1) release the Undivided Interest to any Person or (2) retain the Undivided Interest and sell power and energy from its Generation Entitlement Share, then after the Lessor has received (x) in the case of clause (1) above, net rents (after reduction for expenses incurred by the Lessor in connection therewith) in an aggregate amount (when discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) equal to 23.5% of Facility Cost, as adjusted to reflect inflation or deflation from the Closing Date to the time of determination (the Adjusted Base Amount), or (y) in the case of clause (2) above, net electric revenues (after reduction for expenses incurred by the Lessor in earning such revenues) in an aggregate amount (discounted as aforesaid) equal to the Adjusted Base Amount, the Lessor shall thereafter reimburse the Lessee out of any further net rent received or net proceeds received from the sale of power and energy to the extent that such rent or proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2 (payable on an annual basis with respect to each year or portion thereof during the term of such lease referred to in clause (1) above or such period referred to in clause (2) above during which the Lessor retains the Undivided Interest); provided, however, that when such amount has been paid the Lessor shall have no further obligation to make reimbursement to the Lessee pursuant to this Section 10(b)(3)(viii). (F) In the event that (i) the Facility Lease

shall have expired or terminated on or after December 31, 2015 (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default), (ii) the Lessor shall sell the Undivided Interest to any Person (including the Lessee in connection with the exercise by the Lessee of the purchase option provided by Section 13(c) of the Facility Lease), and (iii) the net sales proceeds (discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) received by the Lessor in connection therewith shall exceed the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above), then the Lessor shall reimburse the Lessee out of the net proceeds of such sale, to the extent that such proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2, whereupon the reimbursement obligation of the Lessor under this Section 10(b)(3)(viii) shall terminate; provided, however, that any such reimbursement shall not reduce the amount of such net sales proceeds retained by the Lessor to an amount (discounted as aforesaid) equal to less than the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above). The reimbursement obligations of the Lessor under clauses (E) and (F) of this Section 10(b)(3)(viii) are for the the sole benefit of the Lessee, and no other Person shall be a third party beneficiary with respect thereto. For purposes of this Section 10(b)(3)(viii), (x) the amount of net rents, net revenues and net sales proceeds attributable to the decommissioning obligation of the Lessee shall be the amount by which such rents, revenues and proceeds are greater than they would have been if the Lessee had had no such obligation, and (y) the amount thereof attributable to the period after the Lease Termination Date shall be the amount determined in the immediately preceding clause

(x) multiplied by a fraction the denominator of which is the number of months in the period commencing May 20, 1986, and ending on the expiration of the economic useful life of Unit 2 as estimated at the time a determination is being made pursuant to this Section 10(b)(3)(viii) and the numerator of which is the number of months in the period commencing on the Lease Termination Date and ending on the expiration of such economic useful life. In the event that the Lessee and the Lessor shall not agree as to the amount of net rents, net electric revenues or net sales proceeds attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date, such amount shall be determined by the Appraisal Procedure. (G) Upon presentation of evidence by the Lessee, reasonably satisfactory to the Equity Participant and the Owner Trustee, that there are amounts then due to pay Decommissioning Cost, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to be delivered pursuant to the Decommissioning Trust Agreement for payment of Decommissioning Cost. (H) Upon presentation of a certificate of a nuclear expert selected by the Lessee and reasonably satisfactory to the Equity Participant and the Owner Trustee, stating that Decommissioning has been completed and all Decommissioning Cost has been paid in full, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to release any funds then remaining in the Decommissioning Trust Fund. (I) Notwithstanding anything in this Participation Agreement or any other Transaction Document to the contrary, the Equity Participant, the Owner Trustee and the Lessee agree to cooperate in amending this Participation Agreement and the Decommissioning Trust Agreement to the extent necessary to enable the Decommissioning Trust Agreement to comply with Section 468A of the Code, or to establish a separate fund meeting the requirements of said Section 468A; provided, however, that in no event shall any

such amendment have a material adverse effect on the Equity Participant's rights in Unit 2 or its security interest in the Decommissioning Trust Fund.

(ix) Letter of Credit. The Lessee shall cause Morgan Bank to issue in favor of the Equity Participant a Morgan Bank irrevocable, transferable letter of credit (such letter of credit and all letters of credit or other credit support instruments issued or executed from time to time in replacement thereof or as a renewal thereof being herein referred to as the Letter of Credit) which, for a term of five years, shall secure the Equity Participant for the payment of Rent due and payable by the Lessee from time to time under the Facility Lease to the extent of the amount available to be drawn under the Letter of Credit at such time. The original stated amount of the Letter of Credit provided by Morgan Bank on the Closing Date shall be \$69,493,938.93, which amount shall be reduced by the amount of each drawing thereunder and shall not be reinstated. The Lessee shall give the Equity Participant notice of the scheduled termination of the Letter of Credit not more than 90 nor less than 60 days before the scheduled termination date. The Lessee agrees to use its best efforts during the Basic Lease Term to renew or replace any expiring Letter of Credit prior to the expiration date thereof with an irrevocable, transferable, unsecured letter or letters of credit having an original stated term of not less than three and not more than eight years, issued by an Eligible Bank or Eligible Banks (the Issuing Bank), or with some other form of credit support acceptable to the Equity Participant in its sole judgment, so that at all times during the Basic Lease Term there shall be a Letter of Credit securing the payment of Rent due and payable by the Lessee from time to time under the Facility Lease to the extent of the amount available to be drawn under the Letter of Credit from time to time. The maximum amount available to be drawn under any replacement Letter of Credit shall be adjusted after each date on which Basic Rent

is due, it being understood, however, that such adjustment shall not take effect until at least ten days after each date on which Basic Rent is due. Any replacement Letter of Credit (1) shall permit partial drawings, (2) shall permit the Equity Participant to assign all or any part of its interest therein without the Issuing Bank's or the Lessee's consent and (3) shall not have termination provisions which are less favorable to the Equity Participant than those of the initial Letter of Credit issued by Morgan Bank. Any reimbursement agreement between the Lessee and the Issuing Bank relating to any replacement Letter of Credit (1) shall not have default provisions which are less favorable to the Lessee than those in the reimbursement agreement for the initial Letter of Credit from Morgan Bank, (2) shall require that the Issuing Bank pay any draws on the Letter of Credit from general funds, and (3) shall not permit the Issuing Bank to exercise its right to set off against any amounts owed as reimbursement to the Issuing Bank for draws on the Letter of Credit. The Lessee shall not grant or permit to exist any Lien on any of its property in favor of the Issuing Bank to secure reimbursement obligations of the Lessee to the Issuing Bank. The Lessee shall not amend any provision of the reimbursement agreement with respect to any Letter of Credit in a manner materially adverse to the interests of the Equity Participant without the prior written consent of the Equity Participant. In addition, if any Eligible Bank (other than Morgan Bank) has its long-term unsecured debt securities (or if it has no long-term unsecured debt securities rated, its long-term deposits) rated less than Aaa by Moody's at the time it issues a Letter of Credit, then if on any biannual anniversary of the date of issuance of such Letter of Credit the credit rating by Moody's of such Bank is below Aa3, within 90 days thereafter the Lessee shall replace such Letter of Credit with one issued by an Eligible Bank. If the Lessee has not secured a commitment for a renewal or replacement Letter of Credit on or prior to the 60th day preceding the stated

expiration date of the Letter of Credit then in effect, or within 10 days after any Issuing Bank shall have given not less than 30 days' notice of the termination of its Letter of Credit prior to its stated expiration date, the Lessee shall notify the Equity Participant of such fact and the Equity Participant shall have the opportunity to find a Person acceptable to it willing to issue a letter of credit for the account of the Lessee on substantially the same terms as the Letter of Credit then in effect, except that the annual fee payable under such replacement letter of credit may be up to 0.375% of the maximum drawable amount under the Letter of Credit. If the Equity Participant has not so found a Person on or prior to the 45th day preceding the stated expiration date of the Letter of Credit then in effect, or within 15 days after any Issuing Bank shall have given not less than 30 days' notice of the termination of its Letter of Credit prior to its stated expiration date, the Lessee shall, unless an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Event of Loss shall have occurred, have the right to purchase the Undivided Interest and the Real Property Interest at any time thereafter on or before the expiration date of the Letter of Credit (exercisable in the same manner as is provided in Section 16(e) of the Facility Lease) for a purchase price equal to the higher of (A) Extraordinary Casualty Value, determined as of the date of purchase, if such date of purchase is a date set forth in Schedule 5 thereto, or the date set forth in such Schedule immediately preceding such date of purchase, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from the date set forth in such Schedule to the date of purchase and (B) the Fair Market Sales Value thereof; provided, however, that if the Lessee shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued Bank Exchange Notes as therein provided), the principal amount of the Notes shall be deducted from the purchase price.

(x) Commercial Operation of Unit 2. On or before September 30, 1987, Unit 2 will have achieved an electric output of not less than 95% of an estimated rated capacity of 1,270 megawatts during a test period of at least 100 consecutive hours.

(xi) Certain Changes to ANPP Participation Agreement. If at any time, through the efforts of APS or otherwise, any of the restrictions on lessors contained in Sections 15.6.3 and 15.8 of the ANPP Participation Agreement are eliminated or reduced for or are made inapplicable to (through amendment, waiver or otherwise) any part of any Generating Unit or Capital Improvement (as such terms are defined in the ANPP Participation Agreement), APS shall cause such restrictions to be comparably eliminated or reduced or made inapplicable to the Lessor. The parties hereto agree to enter into such amendments to this Participation Agreement and the other Transaction Documents and such other instruments and documents as shall be necessary or appropriate to effect the foregoing.

(xii) Intentionally left blank.

(xiii) Limitation on Certain Rights of the Lessee. The Lessee shall not exercise any of its rights under Section 12(a), 12(b) or 13(c) of the Facility Lease unless it is concurrently exercising any similar rights it may have in any other facility leases relating to Unit 2. If the Lessee shall have elected to return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5(a) of the Facility Lease and subsequently determines prior to the Lease Termination Date that it requires additional capacity from PVNGS, before the Lessee concludes any arrangement for such capacity, it shall first give written notice to the Lessor. If the Lessor elects, within 30 days of receipt of such notice, to sell the Undivided Interest and the Real Property Interest to the Lessee, the Lessee shall purchase the Undivided Interest and the Real Property Interest at the Fair Market Sales

Value thereof (determined by agreement of the Equity Participant and the Lessee or, failing such agreement, by the Appraisal Procedure) on the Lease Termination Date. If the Lessor has not made such election prior to the expiration of the period during which the Lessor is entitled to make such election, the Lessee shall be free to conclude such arrangements for capacity from PVNGS as it desires.

(xiv) Additional Financial Reports. The Lessee shall provide, within 120 days after the end of the fiscal year of each ANPP Participant whose net worth is included in the calculation of Net Worth Factor, annual certified financial reports with respect to each such ANPP Participant.

(xv) Other Agreements. The Lessee shall not enter into or become bound by any agreement or arrangement which would proscribe its ability to assume the obligations and liabilities of the Owner Trustee in accordance with Section 3.9(b) of the Indenture or to accept the Special Transfer.

(xvi) ANPP Agreements. If for any reason any of the restrictions on lessors contained in Section 15.6.3, 15.8, or 15.10 of the ANPP Participation Agreement are applicable on the Lease Termination Date or the Lessee shall not have granted to the Lessor a ground lease as contemplated below by the Lease Termination Date, and the effect of such restriction or restrictions is to reduce the amount received by the Lessor upon a disposition (by sale, lease or otherwise) from what would have been realized had such restriction or restrictions not been applicable or had such ground lease been in effect, then the Lessee shall pay to the Lessor an amount equal to such reduction, payable within 10 days after determination of such amount. Such amount shall be determined promptly after the Lease Termination Date by agreement between the Equity Participant and the Lessee or, if they shall be unable to agree within 30 days after the Lease Termination Date, by the Appraisal Procedure.

(xvii) Ground Lease. APS shall use its best efforts to grant a ground lease to the Lessor covering the PVNGS Site (which shall provide for rent of \$1 per year until the expiration of the Lease Term and Fair Market Rental Value thereafter), in which case the Lessor shall simultaneously sell back to the Lessee the realty covered by the Deed for a price equal to the Real Estate Investment. The parties hereto will cooperate in effecting the foregoing.

SECTION 11. Conditions Precedent.

(a) Equity Participant and Agent Conditions. The obligation of (x) the Agent, for the account of the Original Loan Participants, to transfer title to the amount of funds on deposit in the Investment Account equal to the aggregate amount of Loans as contemplated by Section 2(c)(i) to the Indenture Trustee, for the account of the Owner Trustee, on the Closing Date, and (y) the Equity Participant to make the Investment on the Closing Date, shall be subject to the fulfillment, on or prior to the Closing Date, of the following conditions precedent (each instrument, document, certificate, opinion, policy or other writing referred to below to be in form and substance satisfactory to the Agent and the Equity Participant):

(1) Notice of Closing; Transaction Documents. Each shall have received executed copies, or sets of executed counterparts, of the Notice of Closing, each Transaction Document (other than the Tax Indemnification Agreement), the Mortgage Release and such other documents as are contemplated by this Participation Agreement, including the Purchase Documents.

(2) Notice of Amount of Loans. The Agent shall have received from Lessee a certificate specifying the actual aggregate amount of the Loans to be funded at Closing.

(3) Tax Indemnification Agreement. The Equity Participant shall have received an executed copy of the Tax Indemnification Agreement.

(4) Authentication Request, etc. The Owner Trustee shall have delivered to the Indenture

Trustee (x) a request, dated the Closing Date, authorizing the Indenture Trustee to authenticate and deliver to the Agent the Initial Series Notes upon the transfer of the amount of funds on deposit in the Investment Account equal to the aggregate amount of Loans as contemplated by Section 2(c)(i) hereof to the Indenture Trustee, for the account of the Owner Trustee, and (y) the counterpart of the Facility Lease marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART".

(5) ~~Due~~ Authorization, Execution and Delivery. All of the documents described in clauses (1) and (3) of this Section 11(a) shall have been duly authorized, executed and delivered by the respective parties thereto and shall be in full force and effect on the Closing Date, and the Agent and the Equity Participant shall have received evidence as to such authorization, execution and delivery.

(6) Initial Series Notes Transaction; Investment. In the case of the Agent, (A) the Owner Trustee shall have executed, and the Indenture Trustee shall have authenticated and delivered to the Agent, the Initial Series Notes in the respective principal amounts and registrations requested by the Agent and evidencing the Loans made on the Closing Date, and (B) the Equity Participant shall have made the Investment.

(7) Loan. In the case of the Equity Participant, the Agent, on behalf of the Original Loan Participants, shall have made the Loans.

(8) ANPP Administrative Committee. The ANPP Administrative Committee shall have made the finding required by Section 15.6.2 of the ANPP Participation Agreement.

(9) No Violation. The making by the Equity Participant of the Investment and by the Original Loan Participants of the Loans shall not violate any Applicable Law.

(10) No Default. No Default, Event of Default or, in the case of the Agent, Indenture Default or Indenture Event of Default, shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred.

(11) Recording and Filing. The recordations and filings described in Schedule 5 shall have been duly made and all recording and filing fees with respect thereto shall have been paid.

(12) Representations and Warranties of the Equity Participant. The representations and warranties of the Equity Participant set forth in Section 7(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent shall have received a certificate of an officer of the Equity Participant, dated the Closing Date, to such effect.

(13) Opinion of the Equity Participant's Special Counsel. In the case of the Agent, it shall have received a favorable opinion of Cravath, Swaine & Moore, as special counsel for the Equity Participant, dated the Closing Date and addressed to the Agent, in form and substance satisfactory to the Agent.

(14) Representations and Warranties of the Owner Trustee. The representations and warranties of FNB and the Owner Trustee set forth in Section 8(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent and the Equity Participant shall have received a certificate of an officer of FNB and a certificate of the Owner Trustee, dated the Closing Date, to such effect.

(15) Opinion of the Owner Trustee's Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Csaplar & Bok, as counsel for the Owner Trustee, dated the Closing Date and addressed to the Agent and the Equity Participant, in form and substance satisfactory to the Agent and the Equity Participant.

(16) Representations and Warranties of the Indenture Trustee. The representations and warranties of Chemical and the Indenture Trustee set forth in Section 9(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent and the Equity Participant shall have received a certificate of an officer of Chemical and the

Indenture Trustee, dated the Closing Date, to such effect.

(17) Opinion of the Equity Participant's Special NRC Counsel. The Equity Participant shall have received a favorable opinion of Shaw, Pittman, Potts & Trowbridge, as special NRC counsel for the Equity Participant, dated the Closing Date and addressed to the Equity Participant, in form and substance satisfactory to the Equity Participant.

(18) Representations and Warranties of the Lessee. (A) The representations and warranties of the Lessee set forth in Section 10(a), in any other Transaction Document, and in any certificate or other document to which the Lessee is a party, executed or delivered in connection with the transactions contemplated hereby or thereby, shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date and (B) no Deemed Loss Event or Event of Loss shall have occurred and no Default or Event of Default shall have occurred and be continuing and the Agent and the Equity Participant shall have received an Officers' Certificate of the Lessee, dated the Closing Date, to such effect, and to the further effect that (x) there has been no material adverse change in the properties, business, prospects or financial condition of the Lessee since June 30, 1986, and no event has occurred since that date which would materially adversely affect the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document to which it is, or is to be, a party, and (y) there has been no material adverse change or development since June 30, 1986 relating to Unit 2, PVNGS or to nuclear power plants generally which affects the operations of Unit 2 or the value of the Undivided Interest or the financial condition of the Lessee.

(19) Opinion of the Lessee's Special Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, as special counsel for the Lessee, dated the Closing Date and addressed to each such Person, in form and substance satisfactory to the Agent and the Equity Participant.

(20) Opinion of Lessee's Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Snell & Wilmer, as counsel to the Lessee dated the Closing Date and addressed to each such Person, in form and substance satisfactory to the Agent and the Equity Participant.

(21) Opinion of Equity Participant's Special Arizona Counsel. The Equity Participant shall have received a favorable opinion of Meyer, Hendricks, Victor, Osborn & Maledon, dated the Closing Date and addressed to the Equity Participant, in form and substance satisfactory to the Equity Participant.

(22) Opinion of the Equity Participant's Special Tax Counsel. The Owner Participant shall have received a favorable opinion of Shearman & Sterling, dated the Closing Date and addressed to the Equity Participant, with respect to such Federal tax and other tax matters as the Equity Participant may reasonably request.

(23) Opinion of Agent's Counsel. The Agent shall have received a favorable opinion of Morrison & Foerster, dated the Closing Date and addressed to it, in form and substance satisfactory to the Agent.

(24) Representations and Warranties of Funding Corp. The representations and warranties of Funding Corp set forth in Section 6(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Equity Participant shall have received an Officers' Certificate of Funding Corp, dated the Closing Date, to such effect.

(25) Opinion of Funding Corp's Counsel. Funding Corp shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, dated the Closing Date and addressed to it, in form and substance satisfactory to Funding Corp.

(26) Taxes. All Taxes, if any, payable in connection with the execution, delivery, recording and filing of the Transaction Documents and all the documents and instruments described in Schedule 5, or in connection with the issue and sale of the Initial Series Notes and the making by the Equity

Participant of the Investment and the Real Estate Investment, and all Taxes payable in connection with the consummation of the transactions contemplated hereby and by the other Transaction Documents, shall have been duly paid in full.

(27) Appraisals. The Equity Participant and the Agent shall have received a letter, dated the Closing Date and addressed to the Equity Participant, from Ebasco Business Consulting Company, containing an appraisal of the Undivided Interest, which appraisal shall reflect such appraiser's reasonable conclusion that (w) the fair market value in the hands of the Owner Trustee of the Undivided Interest on the Closing Date, taking into account the effect and existence of the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, is equal to not less than the Purchase Price as set forth in the Notice of Closing, (x) the estimated remaining economic useful life of Unit 2 and of the Undivided Interest is at least 39.309 years, (y) at the expiration of the first 2 years of the Fixed Rate Renewal Term the Undivided Interest will have an estimated residual value, taking into account the effect and the existence of this Participation Agreement, the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, in the hands of the Owner Trustee or a Person (unrelated to the Lessee) who could lease or purchase the Undivided Interest from the Owner Trustee for commercial use, equal to at least 20% of the Purchase Price, determined without including in such value any increase or decrease for inflation or deflation during the period from the Closing Date through the expiration of the first 2 years of the Fixed Rate Renewal Term, and (z) taking into account the effect and the existence of the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, the use of the Undivided Interest at the Lease Termination Date by any User is feasible from an engineering and economic point of view and is commercially reasonable. The Equity Participant shall have received an appraisal of the Real Property Interest, which appraisal shall reflect the appraiser's reasonable conclusion that the fair market value in the hands of the Owner Trustee of the Real Property Interest on the Closing Date is equal to the Real Estate Investment as set

forth in the Notice of Closing and shall cover such other matters as the Equity Participant shall have requested. The Equity Participant shall have received a letter from Ebasco Business Consulting Company discussing certain matters relating to the value of the Common Facilities and the Undivided Interest.

(28) Offering and Sale of Interest. The Agent, the Owner Trustee and the Equity Participant shall have received a letter from The First Boston Corporation and Lease Management Corporation with respect to the offering and sale of the interests in the transactions contemplated by this Participation Agreement.

(29) Governmental Action. The Lessee shall have obtained all Governmental Actions (including, without limitation, the Arizona Order, which order shall be final and non-appealable, and the License Amendment) required or, in the opinion of the Equity Participant and the Agent, advisable for the consummation of all the transactions contemplated by this Participation Agreement and the other Transaction Documents in accordance with their respective terms.

(30) Title Report; Title Insurance. The Equity Participant and the Agent shall have received (i) an updated title report, dated the Closing Date, with respect to the PVNGS Site, which report does not disclose any exceptions materially adverse to the possession or operation of Unit 2 or the performance by the Lessee of its obligations under this Participation Agreement and the other Transaction Documents to which the Lessee is a party; and (ii) such title insurance policies with respect to the PVNGS Site and improvements thereon (including the Owner Trustee's interests therein) as it shall have reasonably requested, such policies to be in form and substance satisfactory to the Equity Participant and the Agent.

(31) No Change or Proposed Change in Tax Laws. No change shall have occurred or been proposed in the Code or any other tax statute, the regulations thereunder or any interpretation thereof that would adversely affect the accuracy of the Tax Assumptions unless such change or proposed change relates to an

alternative minimum tax or the effect of such change or proposed change is provided for in Section 3(d) of the Facility Lease.

(32) Insurance. The Equity Participant shall have received a written report from its independent insurance consultant in form and substance satisfactory to the Equity Participant and a copy thereof shall have been delivered to Agent.

(33) Survey. The Equity Participant and Agent shall have received a survey of the PVNGS Site prepared subsequent to January 1, 1979.

(34) Special Certificate of the Lessee. The Equity Participant and the Agent shall have received a certificate of the Lessee, dated the Closing Date, to the effect that (A) Unit 2 has been in all material respects completed in a good and workmanlike manner and in accordance with the plans and specifications relating thereto (as the same may have been modified from time to time to reflect Unit 2 as actually completed), Applicable Law (including, without limitation, the regulations of the NRC), the License and the ANPP Participation Agreement, (B) all Governmental Actions necessary for the commercial operation of Unit 2 (including the Undivided Interest) have been received, other than any such Governmental Action that is routine in nature for PVNGS or that cannot be obtained under Applicable Law, or is typically not applied for, prior to the time it is required, and that the Lessee reasonably expects to be obtained in due course, (C) the plans and specifications relating to Unit 2 are complete in all material respects (modified or to be modified as aforesaid) and consistent with prudent engineering practice, (D) the testing and startup procedures and the operation and maintenance programs for Unit 2 are consistent with such plans and specifications, Applicable Law and prudent engineering practice, (E) Unit 2 has been tested in accordance with all customary testing and startup procedures which would have been performed on or prior to the Closing Date, and such tests and procedures indicate that Unit 2 will have the capacity and functional ability to perform in commercial operation, on a continuing basis, the function for which it is designed in accordance with such plans and specifications and has a nominal capacity of 1,270 megawatts electric,

(F) all material Governmental Actions relating to the construction, operation or maintenance of Unit 2 are listed in a schedule thereto, (G) there is no present event or condition which would materially adversely affect the capability of Unit 2 to operate in accordance with such plans and specifications and (H) based upon the Lessee's present reasonable expectations, and subject to Applicable Law, the rights and interests made available to the ANPP Participants (including the Lessee) pursuant to the ANPP Participation Agreement, as such rights and interests are made available or are to be made available to the Owner Trustee (or to any successor or assign of the Owner Trustee or any "Transferee" of the Owner Trustee under Section 15.10 of the ANPP Participation Agreement) under and pursuant to this Participation Agreement, the Real Property Interest or the Assignment and Assumption, together with the rights to be made available under and pursuant to the Assignment and Assumption, are adequate to permit, during the period following the Lease Termination Date or the taking of possession of the Undivided Interest and the Real Property Interest in the exercise of remedies under Section 16 of the Facility Lease, in accordance with the ANPP Project Agreements (i) the construction, location, occupation, connection, maintenance, replacement, renewal, repair or removal of Unit 2, (ii) the use, operation and possession of Unit 2, (iii) the construction, use, operation, possession, maintenance, replacement, renewal and repair of all Capital Improvements, (iv) adequate ingress to and egress from Unit 2 for any reasonable purpose in connection with the exercise of rights under the Assignment and Assumption and the ownership and possession of the Undivided Interest and (v) the obtaining of nuclear fuel, of water and of transmission services to the ANPP Switchyard sufficient to enable delivery of the Generation Entitlement Share included in the Undivided Interest in a commercially efficient manner and on commercially reasonable terms. Nothing in the foregoing clause (H) shall be deemed to be or be construed as a warranty by the Lessee as to the performance by the Operating Agent of its obligations under the ANPP Participation Agreement. Such certificate shall also be attested to by Edwin E. Van Brunt, Jr., Executive Vice President, of the Lessee, who shall state that (i) as a qualified engineer, he has made such investigation, inspection

and review as he deems necessary to make the statements in such certificate and (ii) to the best of his knowledge, the statements of the Lessee in such certificate are true and correct.

(35) Other Matters. The Agent and the Equity Participant shall have received such other documents, certificates and opinions as the Agent or the Equity Participant, or their respective counsel, shall reasonably request.

(b) Lessee Conditions. The obligation of the Lessee to sell and lease back the Undivided Interest and the Real Property Interest on the Closing Date pursuant to Section 4 shall be subject to the fulfillment or waiver on or prior to the Closing Date of the following conditions precedent, in each case in form and substance satisfactory to the Lessee:

(1) Paragraph (a) Documents. The Lessee shall have received copies of the documents, certificates, opinions (other than the opinion referred to in Section 11(a) (22)), appraisals, letters and forms described in paragraph (a) of this Section 11. All such opinions shall be addressed to the Lessee, except the opinions referred to in clauses (13), (15), (17), (19), (20), (21), (22) and (23) of said paragraph (a).

(2) Payment of Purchase Price. The Owner Trustee shall have paid to the Lessee an amount, in immediately available funds, equal to the Purchase Price and the Real Property Investment.

(3) Special Opinion of the Lessee's Special Counsel. The Lessee shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, dated the Closing Date and addressed to the Lessee, with respect to such Federal tax and other matters as the Lessee may reasonably request.

(4) Accountant's Letter. The Lessee shall have received a letter satisfactory to it from Deloitte Haskins & Sells, to the effect that, under generally accepted accounting principles and SFAS No. 13, the Facility Lease is an "operating lease".

(5) Order and License Amendment. The Arizona Order and the License Amendment shall be in form and

substance satisfactory to the Lessee and the Arizona Order shall be final and nonappealable.

(c) Conditions to Refundings. In addition to the limitations set forth in Section 2(e), the obligation of the Equity Participant and Funding Corp to participate in a refunding or reoptimization of the any Outstanding Notes, as provided in Section 2(e) or 2(f), shall be subject to the fulfillment on or before the applicable Refunding Date of the following conditions precedent (each instrument, document, certificate, opinion or other writing to be in form and substance satisfactory to Funding Corp and the Equity Participant):

(1) Authentication Request, etc. The Owner Trustee shall have delivered to the Indenture Trustee a request, dated the applicable Refunding Date, authorizing the Indenture Trustee to authenticate and deliver the Refunding Notes to or upon the order of the Loan Participant against redelivery of the Outstanding Notes to the Indenture Trustee for cancellation.

(2) Refunding Notes and Bond Transactions. (A) The Loan Participant shall have received (x) if and to the extent that the Loan Participant is Funding Corp, the proceeds from the sale of Refunding Bonds in an amount sufficient to make the Refunding Loan, and (y) from the Lessee (as a special payment of Basic Rent, if the Refunding Date shall be a date other than June 30 or December 30 of any year), an amount equal to accrued interest on the Outstanding Notes from, and including, the later of the date thereof or the date to which interest thereon shall have been paid, to, but excluding, the applicable Refunding Date, (B) the Owner Trustee shall have executed, and the Indenture Trustee shall have authenticated and delivered, to or upon the order of the Loan Participant the Refunding Notes evidencing the Refunding Loan and (C) if and to the extent that the Loan Participant is Funding Corp, the Collateral Trust Trustee shall have accepted the Refunding Supplemental Indenture subjecting the Refunding Notes to the lien of the Collateral Trust Indenture.

(3) No Default. No Default, Event of Default, Indenture Default or Indenture Event of Default

shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred.

(4) Representations and Warranties. The representations and warranties of the Equity Participant, FNB and the Owner Trustee, and the Lessee set forth in Sections 7(a), 8(a) and 10(a), respectively, shall be true and correct on and as of the applicable Refunding Date with the same effect as though made on and as of such Refunding Date (with all references to the Closing Date in such representations and warranties being changed to a reference to the applicable Refunding Date), and the Loan Participant and the Equity Participant shall have received appropriate certificates, dated the Refunding Date, to such effect (and with respect to paragraph (3) above, in the case of the Lessee) and the Equity Participant, FNB, the Owner Trustee and the Lessee shall provide such additional representations and warranties as of the applicable Refunding Date as the Equity Participant, FNB, the Owner Trustee or the Lessee shall reasonably request.

(5) Registration Statement. If and to the extent that the Loan Participant is Funding Corp, and the Bonds shall be sold in a public offering, the Equity Participant and the Agent, if the Initial Series Notes are being refunded, shall have received an Officers' Certificate of the Lessee, dated the applicable Refunding Date, to the effect that on the date it becomes effective and on the applicable Refunding Date, the Registration Statement did not and does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements contained therein in light of the circumstances under which they were made not misleading.

(6) Opinions of Counsel. The Equity Participant, the Loan Participant and the Lessee shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, as counsel for Funding Corp, dated the Refunding Date and addressed to the Equity Participant, the Owner Trustee, the Indenture Trustee and the Lessee, addressing such matters relating to the transactions in connection with the Refunding Notes as the Equity Participant, the Owner Trustee, the Indenture Trustee or the Lessee may reasonably request. The Equity

Participant shall have received favorable opinions of Cravath, Swaine & Moore, as special counsel for the Equity Participant, Csaplar & Bok, as counsel for the Owner Trustee, Mudge Rose Guthrie Alexander & Ferdon, as special counsel for the Lessee, and Snell & Wilmer, as counsel for the Lessee, each dated the applicable Refunding Date and addressing such matters relating to the transactions in connection with the Refunding Notes as the Loan Participant, the Equity Participant, the Owner Trustee, the Indenture Trustee or the Lessee may reasonably request. The Equity Participant shall have also received an opinion of independent tax counsel, dated the Refunding Date and addressed to the Equity Participant, that the issuance of the Refunding Notes shall not result in any adverse tax effect to the Equity Participant.

(7) Receipt of Documents. If and to the extent that the Loan Participant is Funding Corp, Funding Corp and the Collateral Trust Trustee shall have received copies of all documents previously delivered to the Agent pursuant to Section 11(a).

(8) Satisfaction of Underwriting Agreement Conditions. If and to the extent that the Loan Participant is Funding Corp, all of the conditions precedent to Funding Corp's obligations under any Underwriting Agreement shall have been met or waived by Funding Corp.

(9) Amendments to Documents. The Equity Participant and the Lessee shall have amended the Tax Indemnification Agreement, and the Owner Trustee and the Lessee shall have amended the Facility Lease, so as to take into account the tax treatment of interest (including original issue discount) payable on any Refunding Note or Bond in a manner that is mutually acceptable.

SECTION 12. Consent to Assignment of the Facility Lease; Consent to Indenture.

(a) Consent to Assignment of Facility Lease. The Lessee hereby acknowledges, and consents in all respects to, the assignment of the Facility Lease by the Owner Trustee to the Indenture Trustee under and pursuant to the Indenture and agrees:

(i) to make each payment of Basic Rent and Supplemental Rent due or to become due thereunder to the extent constituting Assigned Payments (excluding, in any event, all Excepted Payments) directly to the Indenture Trustee at the Indenture Trustee's Office, so long as any of the Notes shall be Outstanding and unpaid; and

(ii) not to seek to recover any payment (other than a payment that both the Owner Trustee and the Lessee agree was made in mistake) made to the Indenture Trustee in accordance with the Indenture once such payment is made.

(b) Consent to Indenture. The Lessee hereby consents in all respects to the execution and delivery of the Indenture, and to all of the terms thereof, and the Lessee acknowledges receipt of an executed counterpart of the Indenture; it being understood that such consent shall not be construed to require the Lessee's consent to any future supplement to, or amendment, waiver or modification of the terms of, the Indenture or any Note, except to the extent expressly provided for.

SECTION 13. Lessee's Indemnities.

(a) General Indemnity. The Lessee agrees, whether or not any of the transactions contemplated hereby shall be consummated and whether or not the Facility Lease, any other Transaction Document or any Financing Document shall have expired or have been terminated, to assume liability for, and the Lessee does hereby agree to indemnify, protect, defend, save and keep harmless each Indemnitee, on an After-Tax Basis, from and against, any and all Claims which may be imposed on, incurred by or asserted against any Indemnitee (whether because of an act or omission by such Indemnitee or otherwise and whether or not such Indemnitee shall also be indemnified as to any such Claim by any other Person) in any way relating to or arising out of (i) Unit 2, the Undivided Interest, the Real Property Interest, PVNGS or the PVNGS Site, or any part of any thereof, any ANPP Project Agreement, the issuance or payment of the Bonds or the Notes, this Participation Agreement or any other Transaction Document or any Financing Document (including, without limitation, the performance or enforcement of any of the

obligations and terms hereunder or thereunder), (ii) a disposition of all or any part of the Undivided Interest, the Real Property Interest, Unit 2 or any other interest of the Owner Trustee in connection with any termination of the Facility Lease, or (iii) the design, construction; assembly, manufacture, financing, erection, purchase, acceptance, rejection, ownership, acquisition, delivery, redelivery, nondelivery, transportation, insuring, lease, sublease, preparation, installation, repair, rebuilding, improvement, modification, transfer of title, abandonment, possession, repossession, use, operation, maintenance, condition, sale, return, storage or disposition of the Undivided Interest, Unit 2, the Real Property Interest, any Capital Improvement, the PVNGS Site, any other facilities or property in or on the PVNGS Site or any other interest of the Owner Trustee or the Equity Participant in any thereof or any accident, nuclear incident or extraordinary nuclear occurrence in connection with any thereof (including, without limitation, (A) claims or penalties arising from any violation of law or liability in tort (strict, absolute or otherwise) or from the active or passive negligence of any Indemnatee, (B) loss of or damage to any property or the environment or death or injury to any Person, (C) latent and other defects, whether or not discoverable, (D) any claim for patent, trademark, service-mark or copyright infringement and (E) any claim of any Indemnatee incurred in the administration of this Participation Agreement, any other Transaction Document or any Financing Document and not paid as Transaction Expenses or included in Facility Cost and, if not included in Transaction Expenses, the reasonable fees and disbursements of counsel (including reasonable allocated costs of in-house counsel) and other professionals incurred in connection therewith); provided, however, that the Lessee shall not be required to indemnify any Indemnatee pursuant to this Section 13(a), (1) for any Claim in respect of Unit 2, the Undivided Interest or the Real Property Interest arising from acts or events not attributable to either any act or omission of the Lessee, whether as agent for such Indemnatee or otherwise, or the period on or before the Lease Termination Date, which occur after redelivery of the Undivided Interest and the Real Property Interest to the Owner Trustee in accordance with Section 5 of the Facility Lease, except to the extent expressly provided in any Transaction Document, the ANPP Participation Agreement or any other agreement or undertaking of the Lessee, (2) for any Claim against such Indemnatee

resulting solely from acts which would constitute the willful misconduct or gross negligence of such Indemnitee (unless imputed to such Indemnitee by reason of Unit 2, the Undivided Interest, the Real Property Interest, PVNGS, the PVNGS Site or any other facilities at the PVNGS Site or any occurrence in connection with any thereof or by reason of any act or omission of the Lessee whether as agent for such Indemnitee or otherwise), (3) for any Transaction Expense to be paid by the Owner Trustee pursuant to Section 14(a), (4) for any Claim resulting solely from a transfer by the Owner Trustee or the Equity Participant of all or part of its interest in the Facility Lease, Unit 2, the Real Property Interest or the Undivided Interest other than in connection with any early termination of the Facility Lease or any exercise of remedies under Section 16 thereof or the transfer contemplated by Section 7(b)(4) or the first transfer by the Equity Participant to an Affiliate of the Equity Participant or (5) in the case of any Loan Participant, the Indenture Trustee and the Collateral Trust Trustee, for any Claim based upon an untrue statement or alleged untrue statement or omission or alleged omission in the Registration Statement or any document or agreement in connection with the sale of the Bonds which is based upon information furnished to the Lessee or its agents by such Indemnitee expressly for use therein. To the extent that an Indemnitee in fact receives indemnification payments from the Lessee under the indemnification provisions of this Section 13(a), the Lessee shall be subrogated, to the extent of such indemnity paid, to such Indemnitee's rights with respect to the transaction or event requiring or giving rise to such indemnity, but only so long as such subrogation shall not materially adversely affect the rights of such Indemnitee or any other Indemnitee hereunder. Nothing herein or elsewhere contained shall be construed as constituting a guaranty by the Lessee of the principal of, premium, if any, or interest on the Notes or the Bonds or of the residual value or useful life of the Undivided Interest.

(b) General Tax Indemnity.

(1) Indemnity. All payments by the Lessee in connection with the transactions contemplated by the Transaction Documents shall be free of withholdings of any nature whatsoever (and at the time that the Lessee is required to make any payment upon which any withholding is required, the Lessee shall pay an

additional amount such that the net amount actually received by the Person entitled to receive such payment will, after such withholding, equal the full amount of the payment then due) and shall be free of expense to each Indemnatee for collection or other charges. If, for any reason, the Lessee is required to make any payment to a taxing authority with respect to, or as a result of, any withholding tax imposed on an Indemnatee by way of withholding from payments to such Indemnatee in respect of the transactions contemplated by the Transaction Documents, which withholding tax is not the responsibility of the Lessee under this Section 13(b) as determined pursuant to this Section 13(b) but without regard to the immediately preceding sentence of this Section 13(b)(1), then such Indemnatee shall pay to the Lessee on an After-Tax Basis an amount which equals the amount paid by the Lessee with respect to, or as a result of, such withholding tax. Whether or not any of the transactions contemplated hereby are consummated, except as provided in Section 13(b)(2), the Lessee shall pay, and shall indemnify, defend and hold each Indemnatee harmless, on an After-Tax Basis, from and against, any and all Taxes howsoever imposed (whether imposed on or with respect to the Indemnatee, the Lessee, Unit 2, the Undivided Interest, the Retained Assets, the Real Property Interest, any Capital Improvement or the PVNGS Site or any part thereof or interest therein or otherwise) by any Federal, state or local government or subdivision thereof or taxing authority in the United States of America or by any foreign country or subdivision thereof or by any foreign or international taxing authority in connection with or relating to (A) the design, construction, financing, purchase, acquisition, acceptance, rejection, delivery, nondelivery, transportation, ownership, assembly, possession, repossession, operation, use, condition, maintenance, repair, improvement, sale, return, storage, abandonment, redelivery, manufacture, insuring, leasing, subleasing, modification, transfer of title, rebuilding, rental, importation, exportation or other application or disposition of, or the imposition of any Lien other than, in the case of the Equity Participant, Equity Participant's Liens and, in the case of the Lessor, Lessor's Liens (or incurrence of any liability to refund or pay over any amount as a result of any Lien other than Equity Participant's Liens and Lessor's Liens) on,

Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof or interest therein, (B) the payment of Rent or the receipts or earnings arising from or received with respect to, and the indebtedness with respect to, Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof, interest therein or application or disposition thereof, (C) any amount paid or payable pursuant to this Participation Agreement, any other Transaction Document or any Financing Document or the transactions contemplated hereby or thereby, (D) Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof, or interest therein, or the applicability of the Facility Lease to the Undivided Interest or any Capital Improvement, or any part thereof or interest therein, (E) this Participation Agreement, any other Transaction Document or any Financing Document or (F) otherwise with respect to or in connection with the transactions contemplated by this Participation Agreement, any other Transaction Document or any Financing Document.

(2) Exclusions from General Tax Indemnity. Section 13(b)(1) (except for the first two sentences thereof) shall not apply to:

(i) Taxes based on, or measured by, net income of an Indemnatee imposed on such Indemnatee by the United States (including, without limitation, any minimum Taxes, capital gains Taxes, any Taxes on, or measured by, items of tax preference, surcharges, additions to tax, penalties, fines or other charges in respect thereof);

(ii) Taxes (other than sales, use or rental Taxes) imposed on an Indemnatee by any state or local government or any subdivision thereof or other taxing authority in the United States or by any foreign country or subdivision thereof or by any foreign or international taxing authority that are based on, or measured by, the net income, items of tax preference, net worth or capital of such

Indemnatee (Income/Capital Taxes), except, with respect to the Equity Participant and any Affiliate thereof and the Trust Estate, any such Income/Capital Taxes imposed by a jurisdiction as a result of a relation or asserted relation of such jurisdiction to the transactions contemplated by the Transaction Documents or the Financing Documents or as a result of the activities of the Lessee, any ANPP Participant or any Affiliate of any thereof in such jurisdiction; provided, however, that the amount of any Income/Capital Taxes for which the Lessee is obligated to indemnify under the preceding exception shall be calculated on a pro forma basis as the amount by which:

(x) the incremental Income/Capital Taxes which the Indemnatee is obligated to pay in such jurisdiction, calculated as:

(1) the actual amount of Income/Capital Taxes which the Indemnatee is obligated to pay in such jurisdiction (except to the extent that any allocation or apportionment method used by such jurisdiction takes into account the income or activities of business entities organized outside the United States of America), taking into account any actual net operating loss carryovers, reduced by

(2) the amount of Income/Capital Taxes which the Indemnatee would be obligated to pay in such jurisdiction (except to the extent that any allocation or apportionment method used by such jurisdiction takes into account the income or activities of business entities organized outside the United States of America), assuming that the transactions contemplated by the Transaction

Documents and Financing Documents had not occurred, taking into account any net operating loss carryovers that would have been available if such transactions or activities had not occurred:

exceeds

(y) any actual aggregate net reduction in Income/Capital Taxes in all other jurisdictions in which the Indemnatee is subject to tax (whether such reduction results from the operation of allocation or apportionment formulas, from credits or otherwise), such aggregate net reduction calculated as:

(1) the aggregate amount of Income/Capital Taxes which the Indemnatee would be obligated to pay in all other jurisdictions in which such Indemnatee is subject to tax, assuming that the transactions contemplated by the Transaction Documents and Financing Documents had not occurred, reduced by

(2) the actual aggregate amount of Income/Capital Taxes which the Indemnatee is obligated to pay in all other jurisdictions in which such Indemnatee is subject to tax;

provided, further, however, that with respect to any tax based on or measured by capital or net worth, the Lessee's indemnity obligation shall not exceed the incremental portion of such Tax attributable to the transactions contemplated by the Transaction Documents;

(iii) Taxes attributable to the Undivided Interest or the Equity Participant's right in the PVNGS Site created by the Real Property Interest that are imposed with respect to any period after the later of (a) the Lease

Termination Date and (b) the date possession of the Undivided Interest has been delivered to the Lessor and the Real Property Interest has been terminated as provided in Section 5(a) of the Facility Lease, unless such Taxes relate to events occurring or matters arising prior to or simultaneously with such date provided that the Lessee shall have fulfilled all of its obligations under the Facility Lease;

(iv) Taxes on or with respect to an Indemnitee arising from any voluntary transfer (it being understood that the term "voluntary transfer" does not include any transfer provided for in the Transaction Documents or the Financing Documents and does not include any transfer to the Lessee or any Affiliate thereof) by such Indemnitee of any interest in the Undivided Interest, the Real Property Interest, the Trust Estate, the Indenture Estate, the Notes or any other right or interest arising under the Transaction Documents or the Financing Documents, unless an Event of Default has occurred and is continuing, or Taxes arising from an involuntary transfer by such Indemnitee of any such interest arising from a bankruptcy or similar proceeding in which such Indemnitee is the debtor unless such bankruptcy or other proceeding relates to the transactions contemplated by the Transaction Documents;

(v) Taxes imposed on an Indemnitee based on or measured by any fees, commission or compensation received by such Indemnitee for acting as trustee, or for other services rendered, in connection with any of the transactions contemplated by the Transaction Documents or the Financing Documents;

(vi) Taxes in the nature of penalties and interest on or with respect to an Indemnitee arising by reason of such Indemnitee's failure to file proper and timely reports or returns (unless the filing of such reports or returns is the obligation of the Lessee under the Transaction Documents or the Financing Documents) imposed by reason of such

Indemnatee's failure to comply with the laws imposing such Tax or its material failure to comply with its obligations under Section 13(b)(6), unless such failure results from any action of the Lessee or failure by the Lessee to comply with any provision of the Transaction Documents or the Financing Documents, including the failure to provide necessary information;

(vii) Taxes on or with respect to an Indemnatee arising as a result of a material failure of such Indemnatee to fulfill its obligations, if any, with respect to the contest of any claim in accordance with Section 13(b)(4) or to provide the Lessee with information reasonably requested by and not otherwise available to the Lessee to enable the Lessee to complete and file or furnish any report, return or statement in accordance with Section 13(b)(5) if such failure effectively precluded the Lessee from effecting a contest of such claim;

(viii) any Taxes imposed on the Lessor resulting from, or which would not have occurred but for, Lessor's Liens, any Taxes imposed on the Equity Participant resulting from, or which would not have occurred but for, Equity Participant's Liens and any Taxes imposed on the Indenture Trustee which would not have occurred but for Indenture Trustee's Liens;

(ix) any Tax on or with respect to any Indemnatee resulting from the gross negligence or willful misconduct of such Indemnatee (it being understood that no Indemnatee is responsible for determining whether a Tax is payable if such Tax is the responsibility of the Lessee under this Section 13(b));

(x) Taxes imposed on or with respect to a transferee (or subsequent transferee) of an original Indemnatee (other than a transferee or subsequent transferee either of which is an Affiliate of the original Indemnatee) to the extent that the amount of such Taxes exceeds the amount of taxes that would have been

imposed on or with respect to such original Indemnatee but for the transfer to such transferee or, if imposed, would not have been subject to indemnification under this Section 13(b); provided, however, that the exception in this clause shall not apply to any transferee where such transfer shall have occurred during the continuance of an Event of Default; and

(xi) any Tax on or with respect to an Indemnatee resulting from any amendment or modification entered into by such Indemnatee to any Transaction Document or Financing Document if the Lessee is not a party to such amendment or modification or has not consented to such amendment or modification, in each case unless an Event of Default shall have occurred and be continuing;

provided, however, that the foregoing paragraphs (i) through (xi) shall not apply to any Tax imposed on the Loan Participant or the indenture estate under the Collateral Trust Indenture.

(3) Calculation of General Tax Indemnity Payments. If any Indemnatee, other than the Equity Participant or any Affiliate thereof or the Trust Estate, realizes a net permanent tax benefit by reason of the payment of any indemnity under Section 13(b)(1), such Indemnatee shall pay the Lessee, but not before the Lessee shall have made all payments theretofore due to such Indemnatee pursuant to this Section 13(b), an amount equal to the lesser of (x) the sum of such tax benefit plus any other net tax benefit realized by such Indemnatee as the result of any payment made by such Indemnatee pursuant to this sentence (determined in a manner consistent with the definition of After-Tax Basis set forth in Appendix A and with the last sentence of Section 13(b)(6)) and (y) the amount of such payment by the Lessee to such Indemnatee and any other payment by the Lessee to such Indemnatee therefore made pursuant to this Section 13(b) less the aggregate amount of all prior payments by such Indemnatee to the Lessee pursuant to this clause (y) with respect to amounts paid pursuant to Section 13(b)(1), it being intended that no such Indemnatee should realize a net tax benefit pursuant

to this Section 13(b) unless the Lessee shall first have been made whole for any payments by it to such Indemnatee pursuant to this Section 13(b); provided, however, that (A) in computing any permanent tax benefit, such Indemnatee shall be deemed first to have utilized all deductions and credits available to it otherwise than by reason of any payment by the Lessee pursuant to this Section 13(b).

(4) General Tax Indemnity-Contests. If a written claim shall be made against any Indemnatee for any Tax for which the Lessee is obligated pursuant to this Section 13(b), such Indemnatee shall notify the Lessee promptly of such claim, but the failure so to notify the Lessee shall not affect any obligation of the Lessee pursuant to this Section 13(b) except as provided in Section 13(b)(2)(vii) (unless the Lessee is otherwise aware of the existence of such claim). If the Lessee shall request in writing within 30 days after receipt of such notice, such Indemnatee shall in good faith and at the Lessee's expense contest the imposition (including the amount) of such Taxes; provided, however, that such Indemnatee may in its sole discretion select the forum for such contest and determine whether any such contest shall be by (A) resisting payment of such Taxes, (B) paying such Taxes under protest or (C) paying such Taxes and seeking a refund thereof; provided further, however, that (X) such Indemnatee shall not be obligated to contest any claim in which the amount in question is less than \$250,000, (Y) at such Indemnatee's option, such contest shall be conducted by the Lessee in the name of such Indemnatee (subject to the preceding proviso) and (Z) in no event shall such Indemnatee be required or the Lessee permitted to contest the imposition of any Taxes for which the Lessee is obligated pursuant to this Section 13(b) unless (v) the Lessee shall have acknowledged its liability to such Indemnatee for an indemnity payment pursuant to this Section 13(b) as a result of such claim if and to the extent such Indemnatee or the Lessee, as the case may be, shall not prevail in the contest of such claim, (w) such Indemnatee shall have received from the Lessee (i) satisfactory indemnity for any liability, expense or loss arising out of or relating to such contest including, but not limited to, (A) all reasonable legal, accountants' and investigatory fees and disbursements, (B) the amount of any

interest, additions to tax or penalty that may be payable as a result of contesting such claim and (C) if such contest is to be initiated by the payment of, and the claiming of a refund for, such Tax, sufficient funds to make such payment on an After-Tax Basis and (ii) an opinion of independent tax counsel selected by the Lessee and approved by such Indemnatee and furnished at the Lessee's sole expense to the effect that a Reasonable Basis exists for contesting such claim or, in the event of an appeal, that there exists a substantial possibility that an appellate court or an administrative agency with appellate jurisdiction, as the case may be, will reverse or substantially modify the adverse determination, (x) the Lessee shall have agreed to pay on demand all reasonable costs and expenses that such Indemnatee may incur in connection with contesting such claim (including, without limitation, all costs, expenses, losses, reasonable legal and accounting fees, disbursements, penalties, interest and additions to tax), (y) such Indemnatee shall have reasonably determined that the action to be taken will not result in any danger of sale, forfeiture or loss of, or the creation of any Lien (except if the Lessee shall have adequately bonded such Lien or otherwise made provision to protect the interests of such Indemnatee in a manner satisfactory to such Indemnatee) on, Unit 27, the Undivided Interest, the Owner Trustee's interest in the PVNGS Site created by the Real Property Interest, or any part of or interest in any of the foregoing, and (z) if such contest shall be conducted in a manner requiring the payment of the claim, the Lessee shall have paid the amount required. The Lessee agrees to give such Indemnatee reasonable notice of any contest prior to the commencement thereof. If any Indemnatee shall obtain a refund of all or any part of any Taxes paid by the Lessee, or if any such refund would be payable to the Indemnatee in the absence of an offsetting liability for Taxes payable to the taxing authority in question (unless such taxing authority would have been foreclosed from asserting such liability but for the contest of such Taxes), such Indemnatee shall pay the Lessee, but not before the Lessee shall have made all payments theretofore due to such Indemnatee pursuant to this Section 13(b), an amount equal to the lesser of (xx) the amount of such refund, including interest received or receivable and attributable thereto or (yy) such tax

payment by the Lessee to such Indemnatee theretofore made pursuant to this Section 13(b), in either case net of any expenses not already paid or incurred by the Lessee; provided, however, that (I) in computing any permanent tax benefit, such Indemnatee shall be deemed first to have utilized all deductions and credits available to it otherwise than by reason of any payment by the Lessee pursuant to this Section 13(b) and (II) notwithstanding the provisions of this Section 13(b)(4), such Indemnatee shall not be obligated to make any payment to the Lessee pursuant to this Section 13(b)(4) if at the time such payment shall be due a Default or an Event of Default shall have occurred and be continuing under the Facility Lease. An Indemnatee shall not be required to make any payment pursuant to this Section 13(b)(4) before such time as the Lessee shall have made all payments and indemnities then due under the Transaction Documents to such Indemnatee. Notwithstanding anything contained in this Section 13(b)(4) to the contrary, no Indemnatee shall be required to contest any claim if the subject matter thereof shall be of a continuing nature and shall have previously been adversely decided pursuant to the contest provisions of this Section 13(b)(4) unless there shall have been a change in the law (including, without limitation, amendments to statutes or regulations, administrative rulings and court decisions) after such claim shall have been so previously decided, and such Indemnatee shall have received an opinion of independent tax counsel selected by the Lessee and approved by such Indemnatee and furnished at the Lessee's sole expense to the effect that such change provides a Reasonable Basis for the position which such Indemnatee and the Lessee, as the case may be, had asserted in such previous contest. Nothing contained in this Section 13(b) shall require any Indemnatee to contest or permit the Lessee to contest a claim which it would otherwise be required to contest pursuant to this Section 13(b) if such Indemnatee shall waive payment by the Lessee of any amount that might otherwise be payable by the Lessee under this Section 13(b) by way of indemnity in respect of such claim.

(5) General Tax Indemnity-Reports. If any report, return or statement is required to be filed with respect to any obligations of the Lessee under or arising out of this Section 13(b), the Lessee

shall timely file the same, except for any such report, return or statement which such Indemnatee has notified the Lessee that it intends to file. The Lessee shall either file such report, return or statement so as to show the ownership of the Undivided Interest in the Owner Trustee and send a copy of such report, return or statement to the Owner Trustee and such Indemnatee or, where not so permitted, notify the Owner Trustee and such Indemnatee of such requirement and prepare and deliver such report, return or statement to the Owner Trustee and such Indemnatee in a manner satisfactory to the Owner Trustee and such Indemnatee within a reasonable time prior to the time such report, return or statement is to be filed or, where such return, statement or report shall be required to reflect items in addition to any obligations of the Lessee under or arising out of this Section 13(b), provide the Owner Trustee and such Indemnatee with information sufficient to permit such return, statement or report to be properly made with respect to any obligations of the Lessee under or arising out of this Section 13(b) (and the Lessee shall hold each Indemnatee harmless from and against any liabilities, obligations, losses, damages, penalties, claims, actions, suits and reasonable costs arising out of any insufficiency or inaccuracy in any such return, statement, report or information). Upon reasonable request by the Lessee, an Indemnatee shall furnish the Lessee with information in the Indemnatee's possession or reasonably obtainable by it (and not otherwise available to the Lessee) necessary for the Lessee to complete any report, return or statement to be filed or furnished by the Lessee. The Lessee shall not have any right to examine the tax returns of any Indemnatee.

(6) General Tax Indemnity-Payment. All Taxes shall be paid when due and payable and, unless otherwise requested by the appropriate Indemnatee, the Lessee shall pay any Taxes for which it is liable pursuant to this Section 13(b) directly to the appropriate taxing authority and shall pay such Indemnatee promptly on demand in immediately available funds any amount due such Indemnatee pursuant to this Section 13(b) with respect to such Taxes. Any such demand shall specify in reasonable detail the payment and the facts upon which the right to payment is based. Each Indemnatee shall promptly

forward to the Lessee any notice, bill or advice received by it concerning any Taxes. Within 30 days after the date of each payment by the Lessee of any Taxes, the Lessee shall furnish the appropriate Indemnatee the original or a certified copy of a receipt for the Lessee's payment of such Taxes or such other evidence of payment of such Taxes as is acceptable to such Indemnatee. The Lessee shall also furnish promptly upon request such data as any Indemnatee may require to enable such Indemnatee to comply with the requirements of any taxing jurisdiction. Whenever any payment is to be made by the Lessee under this Section 13(b) and it shall be necessary, in calculating the After-Tax Basis amount of such payment, to compute the amount of any liability for federal, state or local tax imposed on or measured by the net income of any Indemnatee, such computation shall be based on the assumption that such taxes shall be payable at the highest marginal statutory rate in effect for the relevant period.

(7) Definition of Indemnatee. For purposes of this Section 13(b), the term Indemnatee shall mean and include the successors and assigns of each respective Indemnatee, and for purposes of federal income taxes, the affiliated group of corporations and each member thereof (within the meaning of Section 1504 of the Code) of which such Indemnatee is a member, if such group shall file a consolidated United States federal income tax return, and, for purposes of income or franchise taxes imposed by a particular state or local taxing jurisdiction, shall mean and include any consolidated or combined group of which such Indemnatee is or shall be a member that is treated as such by such state or local taxing jurisdiction.

(c) Supporting Material. Each Indemnatee shall provide to the Lessee such supporting material (other than tax returns) as the Lessee shall reasonably request in connection with the matters set forth in Section 13(b). The Lessee shall reimburse to any Indemnatee any expenses reasonably incurred in providing requested supporting material to the Lessee.

(d) Cooperation. The Equity Participant shall cooperate and shall cause the Owner Trustee to cooperate with and to consider in good faith any reasonable

request by the Lessee upon the written request and at the expense (including a reasonable allowance for internal costs of the Equity Participant) of the Lessee, in order to avoid or minimize any Taxes for which the Lessee is responsible under Section 13(b).

SECTION 14. Transaction Expenses.

(a) Transaction Expenses. Subject to the provisions of paragraph (c) of this Section 14, with funds provided by the Equity Participant, the Owner Trustee hereby agrees that it will pay when due an appropriate portion (taking into account the other undivided interests in Unit 2 being sold on the Closing Date) of the following costs and expenses (Transaction Expenses) without duplication of amounts payable with respect to other undivided interests in Unit 2 sold on the Closing Date:

(i) the reasonable legal fees and disbursements of Morrison & Foerster, Cravath, Swaine & Moore, Morgan, Lewis & Bockius, Shearman & Sterling, Csaplar & Bok, Shaw, Pittman, Potts & Trowbridge, Meyer, Hendricks, Victor, Osborn & Maledon, Davis Polk & Wardwell and White & Case (as counsel for the Indenture Trustee) for their services rendered in connection with the execution and delivery of this Participation Agreement and the other Transaction Documents and all fees, expenses and disbursements incurred by them in connection with such transactions;

(ii) the initial (but not the ongoing) fees and expenses of the Owner Trustee and the Indenture Trustee;

(iii) all stenographic, printing, reproduction, and other reasonable out-of-pocket expenses (other than investment banking or brokerage fees) incurred in connection with the execution and delivery of this Participation Agreement and the other Transaction Documents and all other agreements, documents or instruments prepared in connection therewith (including all computer analysis and travel related costs);

(iv) the fees and expenses of the appraisers for services rendered as contemplated by Section 11(a)(27), the insurance consultant for services rendered as contemplated by Section 11(a)(32), and such other special counsel or consultants as the Equity Participant may require and shall be identified to the Lessee prior to the Closing Date;

(v) all costs of issue of the Bonds issued to refund the Initial Series Notes including, without limitation, the costs of preparing the Financing Documents, all filing fees relating to any Registration Statement and the fees, expenses and disbursements of White & Case, as counsel for the Collateral Trust Trustee, Morrison & Foerster, as counsel for the Agent, and Sullivan & Cromwell, as counsel for the purchasers, or in the event of a public offering of such Bonds, underwriters, of the Bonds, the initial fees of the Collateral Trust Trustee and its out-of-pocket expenses through the applicable Refunding Date, rating agency fees, the fees and commissions of the underwriters of such Bonds and the fees, expenses and disbursements of the Loan Participant; and

(vi) the fees and out-of-pocket expenses of The First Boston Corporation and Lease Management Corporation in connection with the placement of the beneficial interest in the Trust, and the fees referred to in Sections 2(c)(ii) and 2(c)(iii).

Subject to the provisions of paragraph (c) of this Section 14, funds for the payment of Transaction Expenses will be provided by the Equity Participant to the Owner Trustee and the Owner Trustee will promptly disburse such funds.

To the extent not included in Closing Date Transaction Expenses which are disbursed as provided in Section 4(a)(ii), the Owner Trustee shall pay, with funds provided by the Equity Participant, an appropriate portion of Transaction Expenses (other than those referred to in clause (v) above) for which invoices or other requests for payment are received on or prior to November 26, 1986. Such payments shall be disbursed on the first Business Day following the 26th day of each

month, commencing with the month in which the Closing Date occurs, in accordance with payment instructions received from the Lessee. The Lessee shall pay all such Transaction Expenses thereafter; provided, however, that the obligation of the Lessee to pay any such Transaction Expenses shall be discharged, pro tanto, to the extent of any such Transaction Expenses actually paid by the Owner Trustee to the parties entitled thereto.

(b) Post-Closing Expenses. The Lessee will pay, on an After-Tax Basis, as Supplemental Rent, (i) the ongoing fees, expenses, disbursements and costs (including legal and other professional fees and expenses) of or incurred by the Owner Trustee, the Indenture Trustee and the Collateral Trust Trustee, including in connection with the issue, sale and purchase of Notes and Bonds after the Closing Date, and (ii) all fees, expenses, disbursements and costs (including legal and other professional fees and expenses including, without limitation, legal and other professional fees and expenses incurred by Agent (including reasonable allocated costs of in-house counsel)) incurred by the Loan Participants, the Equity Participant (including internal costs of the Equity Participant), the Owner Trustee, the Indenture Trustee and the Collateral Trust Trustee in connection with (a) any Default, Event of Default, Indenture Default or Indenture Event of Default, (b) the entering into or giving or withholding of any amendment, modification, supplement, waiver or consent with respect to any Transaction Document or Financing Document, (c) any Event of Loss or Deemed Loss Event, (d) any transfer of all or any part of the right, title and interest of the Indenture Trustee in, to and under the Transaction Documents, (e) any transfer of all or any part of the right, title and interest of the Owner Trustee in the Undivided Interest, the Real Property Interest or in, to and under the Transaction Documents, (f) any transfer contemplated by Section 7(b)(4) and (g) any releveraging, refunding or reoptimization referred to in Section 2(d), 2(e) or 2(f) (except to the extent constituting Transaction Expenses).

(c) Lessee's Obligation. Notwithstanding Section 14(a), in the event the transactions contemplated by this Participation Agreement shall not be consummated, the Lessee shall pay or cause to be paid, and shall indemnify and hold harmless the Agent and Original Loan Participants, the Indenture Trustee, the Owner

Trustee and the Equity Participant in respect of all Transaction Expenses other than the fee of Lease Management Corporation referred to in clause (vi) of Section 14(a) unless such failure to consummate shall result solely as a result of a breach by the Equity Participant.

SECTION 15. Equity Participant's Transfers.

(a) Transfers. After the Closing Date (except as provided in Section 7(b)(4)) the Equity Participant shall not assign, convey or otherwise transfer all or any part of (including, without limitation, an undivided interest in) its right, title or interest in and to this Participation Agreement, any of the other Transaction Documents or the Trust Estate (except its right to receive Excepted Payments) to any Person (a Transferee) except on the following conditions:

(i) the Transferee shall enter into an agreement or agreements whereby such Transferee confirms that it shall be bound by the terms of this Participation Agreement and each other Transaction Document, to the extent of the interest transferred, as if it had been originally named as the Equity Participant hereunder and thereunder;

(ii) the Transferee shall be a financial institution, a corporation or a partnership composed of financial institutions or corporations; and

(iii) such transfer shall not violate the Securities Act or any provision of, or create a relationship which would be in violation of, any Applicable Law or agreement to which the transferring Equity Participant or the Transferee is a party or by which its property is bound.

Upon any such transfer that meets all of the foregoing conditions, the transferring Equity Participant shall be released from its obligations under this Participation Agreement and the other Transaction Documents to the extent of the interest transferred. An agreement to transfer shall not in and of itself constitute a transfer for purposes of this Section 15.

(b) Procedure. If the Equity Participant transfers all or any part of its interest hereunder pursuant to this Section 15, it shall give written notice thereof to the Lessee, the Owner Trustee, the Indenture Trustee and the Loan Participants, specifying the name and address for notices to the Transferee, such other information and evidence as shall be necessary to establish compliance with this Section 15 and the extent of the interest transferred to such Transferee. If, as a result of any such transfer, the original Equity Participant is not to continue to receive all payments to be made by the Indenture Trustee to the "Equity Participant" under the Indenture, the original Equity Participant shall from time to time, by notice to the Indenture Trustee, with copies to the Lessee, the Owner Trustee and the Collateral Trust Trustee, designate the manner in which any such payments to the "Equity Participant" are to be allocated, and the Indenture Trustee shall be entitled to rely on such notice for all purposes. This Section 15 shall not apply to the Special Transfer. This Section 15 is for the benefit of the Lessee, the Owner Trustee and the Equity Participant and may not be enforced by any other party hereto.

SECTION 16. Brokerage and Finders' Fees and Commissions.

Except to the extent of amounts payable by the Equity Participant pursuant to Section 14, the Lessee will indemnify and hold harmless the Loan Participants, the Indenture Trustee, the Owner Trustee and the Equity Participant in respect of any commissions, fees, judgments or other expenses of any nature and kind which any of them may become liable to pay by reason of any claims by or on behalf of brokers, finders, agents, advisors or investment bankers in connection with the transactions contemplated by this Participation Agreement, any other Transaction Document, or any litigation or similar proceeding arising from any such claims, other than those claims arising out of written undertakings of the party claiming indemnification under this Section 16 or any Affiliate or shareholder (or Affiliate of such shareholder) of such Person with any such broker, finder, agent, advisor or investment banker.

SECTION 17. Survival of Representations and Warranties; Binding Effect.

(a) Survival. All indemnities, representations and warranties contained in this Participation Agreement, in any other Transaction Document, in any Financing Document and in any agreement, document or certificate delivered pursuant hereto or thereto or in connection herewith or therewith, shall survive, and shall continue in effect following, the execution and delivery of this Participation Agreement, the making of the investments and the loans referred to herein, any disposition of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Participation Agreement and the expiration or other termination of any of the Transaction Documents or Financing Documents and shall be and continue in effect notwithstanding (i) any investigation made by the Equity Participant or the Loan Participants or (ii) the fact that any of the Indenture Trustee, the Owner Trustee, the Loan Participants or the Equity Participant may waive compliance with any of the other terms, provisions or conditions of any of the Transaction Documents or Financing Documents. The obligations of the Lessee under Sections 10(b)(1)(vi), 10(b)(1)(vii), 10(b)(2), 10(b)(3)(iv), 10(b)(3)(vii), 10(b)(3)(viii), 10(b)(3)(ix), 10(b)(3)(xi), 10(b)(3)(xiii), 10(b)(3)(xv), 10(b)(3)(xvi), 13, 14, 16 and 19(f) shall survive the expiration or other termination of this Participation Agreement or any other Transaction Document or Financing Document; provided, however, that following the payment in full and cancellation of the Initial Series Notes, the Agent and the Original Loan Participants shall have no further rights under, and the Lessee shall have no further obligations to the Agent and the Original Loan Participants under, Sections 7(b)(4), 10(b)(1)(vi), 10(b)(1)(vii), 10(b)(2), 10(b)(3)(iv), 10(b)(3)(vii), 10(b)(3)(viii), 10(b)(3)(ix), 10(b)(3)(xi), 10(b)(3)(xv), 10(b)(3)(xvi) and 17(b). The modification by law of any statute of limitations or the waiver or extension of any statute of limitations by the Owner Trustee, the Indenture Trustee, the Lessee, the Equity Participant, any Loan Participant or any Indemnitee shall not affect such survival.

(b) Binding Effect. All agreements, representations and warranties in this Participation Agreement, the other Transaction Documents and the

Financing Documents and in any agreement, document or certificate delivered concurrently with the execution of this Participation Agreement or from time to time thereafter, shall bind the party making the same and its successors and permitted assigns and shall inure to the benefit of each party for whom made and their respective successors and permitted assigns, and, to the extent provided in the next sentence, each Indemnatee and its successors and assigns. The obligations of the Lessee under Sections 10(b)(3)(viii) and 13 hereof and under Section 20 of the Facility Lease are expressly made for the benefit of, and shall be enforceable by, any Indemnatee, separately or together, without declaring the Facility Lease to be in default and notwithstanding any assignment by the Lessor of the Facility Lease or any of its rights thereunder or any disposition of all or any part of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Participation Agreement; or in this Participation Agreement or any other Transaction Document. All payments required to be made pursuant to Section 10(b)(3)(viii)/or 13 shall be made directly to, or as otherwise requested by, the Indemnatee entitled thereto upon written demand by such Indemnatee. Except to the extent permitted by Section 10(b)(3)(ii), the Lessee shall not assign any of its rights or obligations hereunder without the prior written consent of the Equity Participant, the Agent and the Owner Trustee. Except as otherwise indicated, all references herein to any party to this Participation Agreement and the other Transaction Documents shall include the permitted successors and assigns of such party.

SECTION 18. Notices.

All communications, notices and consents provided for herein shall be in writing, and sent by telex, telecopy or other wire transmission containing a request for assurance of receipt in a manner typical with respect to communications of that type, or mailed by registered or certified mail, or personally delivered, and shall be addressed (i) if to the Equity Participant, at 111 East Prospect, Stamford, CT 06904, Attention: President; (ii) if to the Agent, at 555 S. Flower Street, Los Angeles, California 90071, Attention: Mr. Gregory House; with a copy to the Agent at Corporate Service Center North, Department No. 1233, 1850 Gateway Blvd., Concord, California 94520, Attention: Ms. Julie Hopkins (Arizona Public Service Company); (iii) if to

Funding Corp, at Corporation Trust Center, 1209 Orange Street, Wilmington Delaware 19801, Attention: President; (iv) if to FNB, or the Owner Trustee, at 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate Trust Division (TWX No. 940581); (v) if to the Indenture Trustee, at 55 Water Street, New York, New York 10041, Attention of Corporate Trust Administration; and (vi) if to the Lessee, at 411 North Central Avenue, P.O. Box 53999, Phoenix, Arizona 85072-3999, Attention: Secretary; or at such other address as any party hereto may from time to time designate by notice duly given in accordance with the provisions of this Section to the other parties hereto. All such communications, notices and consents given in the manner provided above shall be effective on the date of receipt of such communication or notice.

SECTION 19. Miscellaneous.

(a) Execution. This Participation Agreement may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Participation Agreement is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Participation Agreement shall be effective on the latest of such dates.

(b) Intention of the Owner Trustee and the Equity Participant. Each of the Owner Trustee and the Equity Participant intends to exercise its rights and carry out its obligations hereunder and under the other Transaction Documents solely with a view to furthering its own best interests and does not have, and does not expect to have, any form of joint profit motive with any other Person. The Owner Trustee and the Equity Participant shall not be required to share any Rent to which they are entitled under the Facility Lease, or the residual value of the Undivided Interest or the Real Property Interest, with any other Person. The Owner Trustee and the Equity Participant are not under the control of nor shall they be deemed to be under the control of any other Person having any interest in Unit 2, and shall not be the agent of or have a right or power to bind any such Person (other than the Equity

Participant as regards the Owner Trustee) without its express written consent. The Owner Trustee (on behalf of the Equity Participant) and the Equity Participant (on its own behalf) have and at all times shall retain the right separately to take or dispose of the Undivided Interest and the Real Property Interest, subject only to the rights of the Lessee, the Indenture Trustee and the Loan Participants under the Transaction Documents. The Owner Trustee and the Equity Participant accordingly do not intend to create any form of partnership or joint venture with any other Person by virtue of the transactions contemplated hereby or by any of the Transaction Documents. In the event that it is determined, contrary to the intent of the Owner Trustee and the Equity Participant, that, for purposes of the Code or any other income tax law, a form of partnership or joint venture exists between the Owner Trustee or the Equity Participant and any other Person, the Owner Trustee and the Equity Participant hereby elect to the extent permitted by law (i) not to have the partnership provisions of the Code or such other income tax law apply to any of the transactions contemplated hereby or by any of the Transaction Documents and (ii) to be treated solely as owning the Undivided Interest and the Real Property Interest.

(c) Governing Law. This Participation Agreement has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York.

(d) Amendments, Supplements, etc. Neither this Participation Agreement nor any of the terms hereof may be amended, supplemented, waived or modified orally, but only by an instrument in writing signed by the party against which enforcement of such change is sought.

(e) Headings. The headings of the sections and paragraphs of this Participation Agreement have been inserted for convenience of reference only and shall in no way restrict or otherwise modify any of the terms or provisions hereof.

(f) Bankruptcy of Equity Participant. If (a) the Equity Participant or the Owner Trustee becomes a debtor subject to the reorganization provisions of the Bankruptcy Code, or any successor provision, (b) pursuant to such reorganization provisions the Equity Participant or the Owner Trustee is required, by

reason of the Equity Participant being held to have recourse liability directly or indirectly to the Holder of any Note or the Indenture Trustee, to make payment on account of any amount payable as principal or interest on such Note and (c) such Holder or the Indenture Trustee actually receives any Excess Amount which reflects any payment by the Equity Participant on account of clause (b) of this Section, then such Holder or the Indenture Trustee, as the case may be, shall promptly refund to the Equity Participant such Excess Amount. For purposes of this Section, "Excess Amount" means the amount by which such payment exceeds the amount which would have been received on or prior to the date of such payment by such Holder or the Indenture Trustee if the Equity Participant or the Owner Trustee had not become subject to the recourse liability referred to in clause (b) of this Section. Nothing contained in this Section shall prevent such Holder or the Indenture Trustee from enforcing any personal recourse obligation (and retaining the proceeds thereof) of the Equity Participant expressly provided for under this Participation Agreement.

(g) Entire Agreement. This Participation Agreement, the other Transaction Documents and the Financing Documents supersede all prior agreements, written or oral, between or among any of the parties hereto relating to the transactions contemplated hereby and thereby and each of the parties hereto represents and warrants to the others that this Participation Agreement and the other Transaction Documents and the Financing Documents constitute the entire agreement among the parties relating to the transactions contemplated hereby and thereby.

(h) Publicity. Each party hereto agrees that it will not issue or release for external publication any article or advertising or publicity matter relating to the transactions contemplated hereby or any similar transaction and mentioning or implying the identity of the Equity Participant without the prior written consent of the Equity Participant; provided, however, that the Equity Participant agrees that such consent shall not be withheld if such disclosure is required by Applicable Law.

(i) Capacity of Lessee. In addition to being an ANPP Participant, APS is also the Operating Agent for PVNGS. The Lessor understands and agrees that APS has

certain duties and responsibilities as such Operating Agent under Applicable Law, as well as to the ANPP Participants under the ANPP Project Agreements, and that the obligations of the Lessee hereunder shall not be interpreted as imposing any additional obligation on APS as a result of its status as Operating Agent.

(j) Annex. If and so long as any Initial Series Note shall be and remain Outstanding, the provisions, terms and conditions set forth in Annex A attached hereto shall be and remain in full force and effect and, shall be incorporated into this Participation Agreement, and if any such provisions, terms or condition shall, or shall be construed to, conflict or be inconsistent with any other provision, terms or condition of this Participation Agreement, the former shall prevail and control for all purposes.

(k) Amendment to Appendix. The parties hereto agree to amend the Facility Lease, the Indenture, the Assignment and Assumption and the Deed and Bill of Sale by replacing Appendix A thereto with the form of Appendix A attached hereto.

(l) Lease Amendment. The parties hereto agree to execute an amendment and supplement to the Facility Lease and to file and record such amendment and supplement in all offices in which the Facility Lease was filed or recorded to give effect to the following agreements:

(1) Section 12(b) of the Facility Lease shall be amended to read in its entirety as follows:

(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period not to exceed 2 years (herein referred to as the Fair Market Renewal Term; and the Fixed Rate Renewal Term (including any

extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in which case Basic Rent payable during such Fair Market Renewal Term shall be as set forth in Section 3(a)(iv).

.SECTION 20. Section 48(d) Election.

Neither the Equity Participant nor the Owner Trustee makes any representation or warranty to the Lessee or any other Person as to the availability or amount of any investment tax credits with respect to the Undivided Interest, except that the Equity Participant hereby agrees with the Lessee that:

(a) Within 60 days after the execution of this Participation Agreement, the Equity Participant will complete and file with the Lessee a statement in the form of Appendix C hereto (the Section 48(d) Election) executed by the Equity Participant, the Owner Trustee and the common parent (the Common Parent) of the affiliated group of corporations of which the Equity Participant is a member (the Group);

(b) The Equity Participant will attach and will cause the Common Parent and direct the Owner Trustee to attach to their respective Federal income tax returns and to the consolidated Federal income tax return of the Group for their respective taxable years in which the Facility Lease commences a summary statement in the form of Appendix D hereto (the Summary Statement);

(c) The Equity Participant will keep and will cause the Common Parent and direct the Owner Trustee to keep the Section 48(d) Election as part of their respective records; and

(d) The Equity Participant will not transfer its interest in the Trust Estate, and will not cause the Owner Trustee to transfer the Undivided Interest, at any time during the Lease Term when a loss or recapture of investment tax credits would occur, to a Person whose status as lessor of the Undivided Interest would result in the loss or recapture of any investment tax credits claimed by the Lessee with respect to the Undivided Interest; provided, however, that if the Equity Participant gives the Lessee notice of a proposed transfer and the Lessee fails to object to the transfer

on such grounds within 30 days of such notice, then the completion of such proposed transfer will not be considered a violation of this covenant.

IN WITNESS WHEREOF, the parties hereto have each caused this Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.

EMERSON FINANCE CO.

By _____
President

Date: August 18, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Banks

By: _____
Title: _____

By: _____
Gregory House
Assistant Vice President

Date: August 18, 1986

PVNGS FUNDING CORP., INC.

By _____
Vice President

Date: August 18, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Vice President and Treasurer

Date: August 18, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner
Trustee

By: _____
Assistant Vice President

Date: August 18, 1986

CHEMICAL BANK, in its indi-
vidual capacity and as
Indenture Trustee

By _____
Vice President

Date: August 18, 1986

Schedule 1

ARIZONA PUBLIC SERVICE COMPANY
PALO VERDE NUCLEAR GENERATING
STATION UNIT 2

<u>BANK</u>	<u>LOAN PERCENTAGE</u>
Bank of America National Trust and Savings Association	10.304178270
Mellon Bank, N.A.	7.212924750
The Chase Manhattan Bank, N.A.	6.182506930
Chemical Bank	6.182506930
Citibank, N.A.	6.182506930
Continental Illinois National Bank and Trust Company	6.182506930
First Interstate Bank of California	6.182506930
Marine Midland Bank, N.A.	6.182506930
The Bank of New York	4.121671285
Irving Trust Company	4.121671285
Wells Fargo Bank	4.121671285
The Arizona Bank	2.060835645
Credit Suisse	2.060835645
The First National Bank of Boston	2.060835645
NCNB National Bank of North Carolina	2.060835645
United Bank of Arizona	2.060835645
The Valley National Bank of Arizona	1.030417820

Schedule 2

ARIZONA PUBLIC SERVICE COMPANY

PALO VERDE NUCLEAR GENERATING
STATION UNIT 2

NOTICE OF CLOSING

EMERSON FINANCE CO.

Pursuant to Section 5(a) of the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among Emerson Finance Co., as Equity Participant, Bank of America, National Trust and Savings Association, for itself and as agent for the Banks referred to in Schedule 1 of the Participation Agreement, PVNGS Funding Corp., Inc., The First National Bank of Boston, as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, and Arizona Public Service Company, as Lessee, Arizona Public Service Company hereby gives notice of a Closing to occur at 10:00 a.m. on August 18, 1986 (the Closing Date). The Closing will be held at the offices of Mudge Rose Guthrie Alexander & Ferdon, 180 Maiden Lane, New York, New York 10038.

(i) Purchase Price is \$

(ii) Real Estate Investment is \$

(iii) The maximum aggregate amount of the Loans is \$

(iv) Based upon information supplied to Arizona Public Service Company, Closing Date Transaction Expenses are an aggregate of [\$]. Instructions with respect to such Closing Date Transaction Expenses are attached hereto.

(v) Payment of the Purchase Price, the Real Estate Investment and the Closing Date Transaction Expenses shall be made pursuant to the Omnibus Transfer Instruction and Receipt dated August __, 1986 (a copy of which is attached hereto).

Capitalized terms used herein and not otherwise specifically defined herein shall have the meanings set forth in Appendix A to the Participation Agreement.

IN WITNESS WHEREOF, Arizona Public Service Company has executed this Notice of Closing this 18th day of August, 1986.

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Paul A. Williams II.

Schedule 3

EQUITY PARTICIPANT INFORMATION; PRICING ASSUMPTIONS

Basic Rent, Casualty Values, Special Casualty Values, Modified Special Casualty Values and Extraordinary Casualty Values, as set forth in the Facility Lease as originally executed, have been computed on the basis of the following pricing assumptions:

1. Investment Percentage: 21.6882455%
2. Loan Percentage: 78.3117545%
3. Interest Rate on Notes: 8% per annum through December 31, 1986 and 10.15% per annum thereafter.
4. Federal ACRS Deductions: 10-year public utility property deductions based on the Purchase Price.
5. Equity Participant's Tax Year-End: September 30, 1986.
6. Closing Date: August 18, 1986.
7. Transaction Expenses: 1.5% of Facility Cost paid by the Equity Participant in addition to its Investment (amortized on a straight-line basis during the Basic Lease Term).
8. Real Estate Investment: .05% of Facility Cost.
9. Basic Rent Payment Date: June 30 and December 30 of each year (rent payable in arrears).

10.	First Basic Rent Payment Date:	June 30, 1987.
11.	Last Basic Rent Payment Date:	December 30, 2015.
12.	Interim Rent Payment Date:	December 30, 1986.
13.	Rent Structure	Semi-Annual Arrears
14.	Equity Participant's Tax Rate	46%
15.	First Estimated Tax Payment Date:	September 15, 1986.
16.	Tax Accounting Method:	Accrual.
17.	Amortization of Notes:	See schedule 4 attached hereto.
18.	Lessor's Portion:	17.9813%
19.	Unit 2 Interest:	5.2326%
20.	Unit 2 Retained Assets Portion:	13.1250%
21.	Facility Cost:	\$200,000,000
22.	Purchase Price:	99.95% of Facility Cost

Schedule 4

Amortization of Initial Series Note

Date	Principal
12/30/1986	0.0000000
6/30/1987	0.3104120
12/30/1987	0.3261654
6/30/1988	0.3427183
12/30/1988	0.3601112
6/30/1989	0.3783869
12/30/1989	0.3975900
6/30/1990	0.4177677
12/30/1990	0.4389694
6/30/1991	0.4612471
12/30/1991	0.4846554
6/30/1992	0.5092517
12/30/1992	0.5350962
6/30/1993	0.5622523
12/30/1993	0.5907866
6/30/1994	0.6207690
12/30/1994	0.6522731
6/30/1995	0.6853759
12/30/1995	0.7201588
6/30/1996	0.7567068
12/30/1996	0.7951097
6/30/1997	0.8354615
12/30/1997	2.0746193
6/30/1998	2.1799062
12/30/1998	2.2905365
6/30/1999	2.4067812
12/30/1999	2.5289254
6/30/2000	2.6572683
12/30/2000	2.7921247
6/30/2001	2.3330862
12/30/2001	1.5109167
6/30/2002	1.8266964
12/30/2002	1.5915723
6/30/2003	1.9269812
12/30/2003	1.6785827
6/30/2004	2.0327636
12/30/2004	1.7703605
6/30/2005	2.1443421
12/30/2005	1.8671670
6/30/2006	2.2620344
12/30/2006	1.9692779
6/30/2007	2.3861754
12/30/2007	2.0769837
6/30/2008	2.5171184

Date	Principal
12/30/2008	2.1905911
6/30/2009	2.6552362
12/30/2009	2.3104234
6/30/2010	2.8009220
12/30/2010	2.4368217
6/30/2011	2.9545903
12/30/2011	2.5701457
6/30/2012	3.1166786
12/30/2012	3.8446815
6/30/2013	2.1523699
12/30/2013	5.8228458
6/30/2014	6.1183553
12/30/2014	3.0208534
6/30/2015	0.0000000
12/30/2015	0.0000000

Schedule 5

Recordations and Filings

Part I. Recordations in Respect of the Sale of, and the Owner Trustee's Title to, the Undivided Interest and the Real Property Interest.

County Recorder, Maricopa County, Arizona:

- (i) Deed;
- (ii) Bill of Sale;
- (iii) Assignment and Assumption;
- (iv) Facility Lease;
- (v) Indenture;
- (vi) Mortgage Release; and
- (vii) Affidavit of Real Property Value.

Part II. UCC-1 Financing Statements.

A. County Recorder, Maricopa County, Arizona:

(i) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease; and

(ii) A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

B. Secretary of State, Arizona:

(i) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease;

(ii) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease to be filed as a public utility; and

(iii) A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

C. Massachusetts/state and local:

A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

Part III. Other Filings.

A. County Recorder, Maricopa County, Arizona:

A partial release on form UCC-2 naming APS, as debtor, and Security Pacific National Bank, as Secured Party.

B. Secretary of State, Arizona:

A partial release on form UCC-2 naming APS, as debtor, and Security Pacific National Bank, as Secured Party.

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof", "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the initial series of Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Aggregate Liability shall mean the amount of Aggregate Liability for a single Nuclear Incident of all Persons Indemnified, as determined in accordance with the Price-Anderson Act.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Adjustment Factor shall mean the quotient obtained by dividing the number of Nuclear Facilities having operating licenses by 100.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive) or accrual of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

Aggregate Liability shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "aggregate liability", the term "Aggregate Liability" shall be similarly expanded.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 13(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes, as amended.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated as of August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under the Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York, Boston, Massachusetts or San Francisco, California are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement is or is not included or reflected in the plans and specifications for Unit 2, as

built, and (b) any alteration, modification, addition or improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation), of any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean a Collateral Trust Indenture among APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS facilities which are common to all generating units, including Unit 2, at PVNGS.

Common Parent shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien

existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Expert shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deed shall mean the Deed, dated as of August 18, 1986, from APS to the Owner Trustee.

Deemed Loss Event shall mean any of the following events (unless and until waived in writing by the Equity Participant):

(1) Utility Regulation. If at any time from and including the Closing Date and before the Lease Termination Date, the Lessor or the Equity Participant, by reason of the acquisition or ownership of the Undivided Interest or the Real Property Interest or any part thereof by the Lessor (or any beneficial interest therein by the Equity Participant) or the lease of the Undivided Interest to the Lessee or any of the other transactions contemplated by the Transaction Documents, shall be deemed by any Governmental Authority having jurisdiction to be, or shall become subject to regulation (other than Non-Burdensome Regulation) as, an electric utility, a public utility or a holding company under any Applicable Law or as a consequence of any Governmental Action, and the effect thereof on the Lessor or the Equity Participant would be, in the sole judgment of the Equity Participant, acting on the advice of counsel, adverse, except that if the Lessee, at its sole cost and expense, is contesting diligently and in good faith any Governmental Action which would otherwise constitute a Deemed Loss Event under this clause (1), such Deemed Loss Event shall be deemed not to have occurred so long as in the sole judgment of the Equity Participant (i) such contest does not involve any danger of the foreclosure, sale, forfeiture or loss of, or the creation of any Lien on, the Undivided Interest, the Real Property Interest or any part thereof or any interest therein, (ii) such contest does not adversely affect the Undivided Interest or the Real Property Interest or any part thereof or any other property, assets or rights of the Lessor or the Equity Participant or the lien of the Indenture thereon, (iii) the Lessee shall have furnished the Equity Participant with an opinion of independent counsel satisfactory to the Equity Participant to the effect that (a) there exists a reasonable basis for contesting such determination or (b) in the case of any action arising from or related to the Lessor or the Equity Participant under the Holding Company Act, it is more likely than not that the Lessee will

successfully contest such determination without the need for any appeal, (iv) such determination shall be effectively stayed or withdrawn during such contest (and shall not in the sole judgment of the Equity Participant be subject to retroactive application at the conclusion of such contest) in a manner satisfactory to the Equity Participant, and the Equity Participant shall have determined in its sole judgment that such contest and the Lessor's continued ownership of the Undivided Interest and the Real Property Interest during the pendency of such contest will not adversely affect its business or the business of any of its Affiliates, and (v) the Lessee shall have indemnified the Lessor and the Equity Participant in a manner satisfactory to the Equity Participant for any liability or loss which either may incur; it being understood, however, that the term Equity Participant as used in this clause (1) does not include any Transferee who at the time of transfer is an entity which is subject to regulation as an electric utility, public utility or a holding company under Applicable Law or Governmental Action.

(2) Change in Applicable Law. Any change in, or new interpretation by a Governmental Authority having jurisdiction relating to, Applicable Law, including, without limitation, the Price-Anderson Act, the Atomic Energy Act, the Nuclear Waste Act or the regulations of the NRC, in each case as in effect on the Closing Date, as a result of which, in the opinion of independent counsel to the Equity Participant: (i) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified is increased; (ii) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified exceeds the amount of Financial Protection required under Applicable Law and available at the time of such Nuclear Incident; (iii) (a) the amount of Primary Financial Protection required with respect to a single Nuclear Facility under Applicable Law is increased, whether or not the total amount of Financial Protection required with respect to a single Nuclear Facility is increased, or (b) the amount of Financial Protection required under Applicable Law is increased (including, but not limited to, an increase in the amount of retrospective premiums payable under the Retrospective Rating Plan) or (c) the amount of

retrospective premiums payable under the Retrospective Rating Plan in any one year with respect to two or more Nuclear Incidents is increased; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. Section 140.22 or 10 C.F.R. Section 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan) shall be modified or changed in any material respect; (v) the Lessor or the Equity Participant may become liable or responsible in any capacity (including, without limitation, through assessments imposed by a Governmental Authority) for payments owed in respect of the Nuclear Waste Fund (as such term is used in Section 302 of the Nuclear Waste Act) or in respect of the handling or disposal of nuclear waste, decontamination, storage, transportation or safekeeping of radioactive or hazardous materials or any other obligation in the nature of the foregoing; (vi) the Lessor, the Equity Participant or the Lessee may be prohibited from asserting any right, protection or defense available under Applicable Law as of the Closing Date with respect to civil or criminal actions brought in connection with a Nuclear Incident (including, without limitation, through an expansion of the waiver of defenses provision under subsection 170n. of the Atomic Energy Act); (vii) there shall be expressly created a new cause of action whereby any Person who pays or will pay retrospective premiums under the Retrospective Rating Plan or other assessments required under Applicable Law may recover the amount of such payments from the facility at which a Nuclear Incident occurs or from any Person associated with such facility; (viii) there shall be a third tier or additional level of potential or real liability (including assessments imposed by a Governmental Authority) with respect to a Nuclear Facility; (ix) there shall be any type of claim, liability or expense (other than the costs of investigating and settling claims and defending suits for damage) excluded from the limitation of liability established by the Price-Anderson Act (through modification of the definitions of "aggregate liability", "persons indemnified", "nuclear incident" or otherwise) or excluded (or the funding or payment thereof deferred) under insurance or other Financial Protection required under Applicable Law as in effect on the Closing Date, except to the

extent and in the amount expressly excluded or deferred pursuant to Applicable Law as in effect on the Closing Date; or (x) the Lessor or the Equity Participant may be exposed, during the Lease Term or after the Lease Termination Date, to any other increased real or potential liability (including, without limitation, through assessments imposed by a Governmental Authority) with respect to a Nuclear Incident or otherwise relating to the operation of PVNGS or the transactions contemplated by the Participation Agreement; provided, however, that no such change shall constitute a Deemed Loss Event if and for so long as such change or interpretation meets all the conditions constituting a Safe Harbor Change. For purposes of this clause (2), the requirement or existence of insurance, retrospective premiums, indemnities (whether by the Lessee or any other Person) or other forms of Financial Protection (similar or dissimilar to the foregoing) shall not be deemed to eliminate or negate any exposure of the Lessor or the Equity Participant to real or potential increased liability.

(3) Insurance. The Lessee shall not be in compliance with Section 10 of the Facility Lease.

(4) License. Any expiration, revocation, suspension, amendment or interpretation by any Governmental Authority of the License or any other change in Applicable Law or Governmental Action, as a result of which, prior to the Lease Termination Date, either the Lessor or the Equity Participant is or might (i) be required to be or become a licensee under the Atomic Energy Act with respect to Unit 2 or (ii) be subject to the obligations or liabilities imposed, as of the Closing Date or thereafter, on licensees under the Atomic Energy Act with respect to Unit 2 or (iii) be otherwise subject to significant regulation.

(5) Multiple Incidents. The occurrence (i) of two or more incidents (including incidents occurring outside the United States of America), in each case at any Nuclear Facility or Facilities using a Combustion Engineering pressurized water reactor nuclear steam supply system or another nuclear steam supply system of comparable design or comparable components, the failure of which Combustion Engineering pressurized water reactor nuclear steam

supply system or other nuclear steam supply system of comparable design or components results in (x) a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; (y) (A) the radiation level in the containment vessel as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equaling or exceeding 1,000 rad per hour; or (B) any measure of radioactivity in the primary coolant system exceeding by 1,000 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (z) damage to offsite property, including, without limitation, costs for decontamination, in amounts in excess of \$15,000,000; or (ii) within a five-year period of three or more incidents, of the type and severity described in subclause (i)(x), (y) or (z) above, at any Nuclear Facility or Facilities (including incidents occurring outside the United States of America).

(6) Illegality; Exercise of Rights and Remedies. Any change in Applicable Law or any Governmental Action the effect of which is or might be (i) to make any of the transactions contemplated by the Transaction Documents unauthorized, illegal

or otherwise contrary to Applicable Law, (ii) to impede the exercise by the Lessor or the Equity Participant of any right or remedy under any Transaction Document relating to the assertion of claims for Rent or monetary damages, (iii) to cause the Lessor or the Equity Participant to be or become liable in any capacity in respect of Decommissioning, including, without limitation, all or any portion of the Termination Obligation (as defined in the ANPP Participation Agreement), or (iv) to constitute an assertion to the effect that (a) the exercise by the Lessor or the Equity Participant of any right (irrespective of the event giving rise to such right) under any Transaction Document would constitute impermissible control over Unit 2 or the licensees of Unit 2, other than an assertion consistent with the second sentence of Section 184 of the Atomic Energy Act and the NRC's regulations thereunder, including, without limitation, 10 C.F.R. Section 50.81, as now in effect, or (b) the acquisition or transfer of the Undivided Interest was in violation of, or otherwise contrary to, Applicable Law.

(7) Violations. With respect to PVNGS, the NRC shall have issued within a two-year period (x) two or more final orders involving "Severity Level I" violations or (y) three or more final orders involving "Severity Level I" or "Severity Level II" violations, as such terms are used in Supplement I to Appendix C to 10 C.F.R., Part 2, as in effect on the Closing Date (or, if such Supplement is amended or superseded or different categories are in effect, comparable violations).

(8) Unit 1 and Unit 3 Incidents. (1) The occurrence of an event at Unit 1 or Unit 3 (such affected unit being herein in this definition referred to as the Affected Unit) as a result of which: (w) the radiation level in the top half of the containment vessel of the Affected Unit as measured by the average of two high range radiation monitors in the upper half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of the Affected Unit shall exceed by 100 times the limiting conditions for operation specified in the

technical specifications for the Affected Unit (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of the Affected Unit's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of the Affected Unit, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date; or (2) the occurrence of a Nuclear Incident at an Affected Unit as a result of which the Affected Unit ceases to operate (or if the Affected Unit is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 36 consecutive months.

(9) Radiation Level. Except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 1 or 3, the radiation level in the fuel building above either such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours.

(10) Reduced Operations. Other than in consequence of a reduction in demand, Unit 2 shall have operated in any calendar year at a net capacity factor below 35% other than as a result of a

shutdown to repair damage to Unit .2; provided, however, that if the NRC shall determine at any time during the Lease Term that the operation of this paragraph might impair the ability of the Lessee or the Operating Agent to comply with the terms of the License or Applicable Law or interfere with the exercise of the NRC's jurisdiction to protect the public health and safety, then this paragraph 10 shall be deemed waived.

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank (as used herein, a Letter of Credit Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Letter of Credit Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Letter of Credit Bank, or (iii) any Letter of Credit Bank whose long-term unsecured debt securities and the long-term unsecured debt securities of any parent company of such Letter of Credit Bank are rated not less than Aa3 by Moody's, other than a Letter of Credit Bank to which the Equity Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of a Letter of Credit Bank which is part of a holding company structure, the failure of such Letter of Credit Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities but eligibility under this clause (iii) shall not be available if the cost of a Letter of Credit issued by an Letter of Credit Bank otherwise qualifying under clause (i) or (ii) for a period of five years shall be greater than the cost of the prior Letter of Credit provided by an Eligible Bank qualifying under clause (i) or (ii)); provided, however, that any Letter of Credit issued by a Letter of Credit Bank that is not incorporated in the United States shall provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Emerson Finance Co., and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended.

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean (i) all indemnity payments to which the Owner Trustee or the Equity Participant (or the respective successors, assigns, agents, officers, directors or employees of the Owner Trustee or the Equity Participant) is entitled, (ii) any amounts payable under any Transaction Document to reimburse the Lessor or the Equity Participant (including the reasonable expenses of the Lessor or the Equity Participant incurred in connection with any such payment) for performing or complying with any of the obligations of the Lessee under and as permitted by any Transaction Document, (iii) any insurance proceeds with respect to an Event of Loss in excess of amounts then due and owing in respect of the principal of and premium, if any, and interest on all Notes Outstanding, (iv) any insurance proceeds (or payments with respect to risks self-insured) under liability policies, (v) any

payments in respect of interest to the extent attributable to payments referred to in clauses (i) through (iv) above and (vi) if the Letter of Credit has been terminated or has expired, a portion of Casualty Value, Special Casualty Value or Extraordinary Casualty Value equal to the amount by which Modified Special Casualty Value exceeds the sum of all amounts drawn under the Letter of Credit.

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and all rights and interests with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank.

Extraordinary Casualty Value, as of any date, during the Basic Lease Term, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under the applicable provision, if any, of the Facility Lease or the Participation Agreement, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Extraordinary Nuclear Occurrence shall have the meaning assigned in Section 11 of the Atomic Energy Act and the related NRC regulations (10 C.F.R. § 140.84 and 140.85), as in effect as of the Closing Date.

Facility Cost shall mean the sum of the Purchase Price and the Real Estate Investment plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement, and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended.

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; (y) any order of or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period exceeding 24 months; or (z) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which: (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications

for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which: (x) the NRC declares to be an Extraordinary Nuclear Occurrence; (y) result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative

criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; or (z) result in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee, or of the Lessee and one or more other ANPP Participants, to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will

exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown in consequence of the occurrence of an event described in (A) clause (4) or (5) above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause (8) above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months.

Financial Protection shall have the meaning assigned in the Price-Anderson Act, as in effect, as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "financial protection", the term "Financial Protection" shall be similarly expanded.

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meaning set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, shall mean the Generation Entitlement Share of APS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all siting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Group shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, each Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture, and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles, a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean that portion of APS's interest in Unit 2 equal to the percentage set forth on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the

Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended, (vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Aggregate Loss shall be computed and applied in respect of Unit 2, including all interests therein, and with respect to each calendar year shall mean the sum of (i) retrospective premiums, if any, payable during such year under the Retrospective Rating Plan with respect to any Nuclear Incident which shall have occurred prior to the date of such calculation, (ii) all uninsured liquidated amounts paid or payable during such year, and not covered by the Retrospective Rating Plan, in respect of Nuclear Incidents, and (iii) other known assessments and costs and an assumed additional amount in respect of such retrospective premiums which would be payable during such year if a Nuclear Incident, or one additional Nuclear Incident, should occur in such year.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of

(x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of the Fixed Rate Renewal Term) in each case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets Portion of the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and (iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets Portion of the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or December 31 in such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

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Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage.

Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions. The after-tax yield component of Net Economic Return will be adjusted upward by 0.1% for each 1% downward adjustment in marginal federal tax rates pursuant to a Change in Tax Law; provided, however, that the maximum upward adjustment due solely to such increase in the after-tax yield component will result in an increase of .20% in the present value of Rent (discounted semi-annually using a semi-annual discount rate equal to 5.075%).

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Net Worth Factor shall mean the quotient obtained by dividing (i) PVNGS Net Worth, as of December 31 of the year prior to the date of any calculation of Net Worth Factor, by (ii) PVNGS Net Worth, as of December 31, 1985; provided, however, that Net Worth Factor shall not be less than 1.0 in respect of any year prior to 1991.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest and the Real Property Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest and the Real Property Interest on or after the Lease Termination Date or

(iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes and Additional Notes issued from time to time under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Facility shall mean a facility designed for producing substantial amounts of electricity and having a rated capacity of 100,000 electrical kilowatts or more.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act, as in effect as of the Closing Date; provided that if the Atomic Energy Act shall be amended to expand the definition of "nuclear incident", the term "Nuclear Incident" shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used.

Original Loan Participants shall mean Bank of America and each of the other banks (the Banks) listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% per annum in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs) or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participants and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's

Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest) under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

Persons Indemnified shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "person indemnified", the term "Persons Indemnified" shall be similarly expanded.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No. 85-256, 71 Stat. 576 (1957), as amended to August 18, 1986 (except as otherwise expressly provided), including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 3 to the Participation Agreement.

Primary Financial Protection shall mean Financial Protection required to be maintained by each Nuclear Facility under Applicable Law, except for such amounts required to be maintained under a Retrospective Rating Plan.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Net Worth shall mean the sum of the consolidated common stockholders equity of APS, El Paso, PNM and Southern California, and their respective successors, as shown in their most recent respective audited financial statements; provided, however, that the consolidated common stockholders equity of any such Person shall not be included in the foregoing sum after (and only after) such time as such Person is not an ANPP Participant subject to the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 4(b) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed or by the ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund the Initial Series Notes or Outstanding Bonds.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean a Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of Refunding Bonds.

Registration Statement shall mean a registration statement, including all exhibits and all documents incorporated in such Registration Statement by reference, filed with the SEC under the Securities Act in connection with the offer, issue and sale of any Refunding Bonds or Refunding Notes.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent.

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Severable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Retrospective Rating Plan shall mean the industry retrospective rating plan established pursuant to the Price-Anderson Act, or any successor or similar plan established under Applicable Law.

Safe Harbor Change shall mean any Substantial Amendment, and any other change which, had it been part of the first Substantial Amendment (together with all other changes since the first Substantial Amendment) would have been a Substantial Amendment, enacted after the Closing Date, if, upon the effective date of such Substantial Amendment or other change and at all times thereafter (as shall be determined from time to time):

(A) (1) the Lessor and the Equity Participant (x) shall, as a result of such Substantial Amendment, be exempt from all real and potential liability in respect of a Nuclear Incident (Nuclear Liability) both during and after the Lease Term (unless the Equity Participant or the Lessor, as the case may be, is as of the time of a Nuclear Incident a licensee with respect to Unit 2 under the Atomic Energy Act) and (y) shall have received an opinion of independent counsel to the Equity Participant to the effect that there is no reasonable basis for a court to hold either the Lessor or the Equity Participant liable for any Nuclear Liability, both during and after the Lease Term (subject to the exception described in the parenthetical clause in clause (x) above) and (2) in the opinion of independent counsel to the Equity Participant, such Substantial Amendment meets all the conditions stated in clause (B) below; provided, however, that part (b) in subclause (i) of clause (B) shall read as follows, "(b) the product of (1) 1.75 times (2) the Net Worth Factor times (3) the product of \$6.5 billion multiplied by the Adjustment Factor***", and subclause (iii) of clause (B) shall read as follows, "Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter shall not exceed the product of (x) 1.75 times (y) .5% times (z) the product of

the Net Worth Factor times \$6.5 billion ***"; provided, further, that in the event the Equity Participant is furnished with an opinion of its independent counsel stating that, because of a change in Applicable Law, there is a significant risk that the opinion described in subclause (y) of subclause (1) above is no longer valid, then this clause (A) shall cease to be applicable; or

(B) in the event clause (A) is not applicable, as a result of such Substantial Amendment, in the opinion of independent counsel to the Equity Participant: (i) Adjusted Aggregate Liability, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed (a) the amount of Financial Protection required to be maintained by each Nuclear Facility with respect to a single Nuclear Incident or (b) the product of (1) the Net Worth Factor times (2) the product of \$6.5 billion times (3) the Adjustment Factor, and if Adjusted Aggregate Liability should exceed either (a) or (b) above the Substantial Amendment shall no longer constitute a Safe Harbor Change; (ii) the amount of Primary Financial Protection available from commercial insurance underwriters on terms substantially equivalent (in the reasonable opinion of the Equity Participant) to the terms in effect on the Closing Date under Applicable Law and required to be maintained by licensees with respect to any single Nuclear Facility shall be at least equal to the amount required under Applicable Law (which amount shall not exceed \$500 million); (iii) Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed the product of (x) .5% times (y) the Net Worth Factor times (z) \$6.5 billion, and if Maximum Aggregate Loss should exceed the foregoing product the Substantial Amendment shall no longer constitute a

Safe Harbor Change; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. § 140.22, or 10 C.F.R. § 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan), as in effect on the Closing Date, shall not have been amended or modified in any material respect; (v) the NRC shall be required to fulfill payment obligations when due from a licensee liable for damage arising out of or related to a Nuclear Incident in the event that the payment obligations of such licensee in any calendar year exceed the amount payable by such licensee in respect of such Nuclear Facility in such year under the Retrospective Rating Plan; provided, however, that the NRC shall be entitled to reimbursement through the Retrospective Rating Plan as such payments are made over time; (vi) neither the Lessee nor any other Persons Indemnified will be required to waive the defense of the statute of limitations (existing under any Applicable Law) with respect to a Nuclear Incident (except an Extraordinary Nuclear Occurrence); with respect to an Extraordinary Nuclear Occurrence such defense shall be required to be waived only as to suits instituted within 30 years after the date the Extraordinary Nuclear Occurrence which is the subject of the suit takes place and within a prescribed number of years from the date on which the claimant first knew, or reasonably could have known, of his injury or damage and the cause thereof; (vii) neither the Lessor nor the Equity Participant shall be exposed to any increased real or potential liability (including assessments imposed by a Governmental Authority) with respect to activities authorized by the Nuclear Waste Act; (viii) none of the results contemplated in subclauses (vii) and (ix) of clause (2) of the definition of Deemed Loss Event shall have occurred; (ix) neither the Lessor nor the Equity

Participant shall, in the opinion of independent counsel to the Equity Participant delivered within six months of such Substantial Amendment, be exposed to any other material increase in its real or potential liability with respect to a Nuclear Incident, either before, on or after the Lease Termination Date, except for liability arising with respect to a Nuclear Incident which takes place after the Lessor or the Equity Participant, as the case may, becomes a licensee of the NRC, and (x) neither the Lessor, the Equity Participant nor the Lessee shall be prohibited from asserting any other right, protection or defense available under Applicable Law as in effect on the Closing Date other than those rights, protections and defenses which are waived pursuant to this definition of Safe Harbor Change; provided, however, that an expansion of the waiver of defenses provision of subsection 170n.(1) of the Atomic Energy Act so that such waivers are applicable with respect to an Extraordinary Nuclear Occurrence arising out of or resulting from or occurring in the course of (a) transportation of source material, byproduct material, or special nuclear material to or from any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, (b) activities undertaken by the Secretary, including but not limited to activities related to the storage or disposal of high-level radioactive waste, or (c) the construction, possession or operation of any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, shall not be deemed to expose the Lessor, the Equity Participant or the Lessee to any increased real or potential liability.

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor, the Equity

Participant and the Indenture Trustee in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Secretary shall mean the Secretary of Energy.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term; the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%)

payable in respect of the Undivided Interest for such Renewal Term (retaining a residual of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted securities ratings.

Summary Statement shall have the meaning set forth in Section 20(b) of the Participation Agreement.

Substantial Amendment shall mean any amendment to the Price-Anderson Act or the Atomic Energy Act which would constitute a Deemed Loss Event under clause (2) of the definition of Deemed Loss Event.

Substituted Lessee shall have the meaning set forth in Section 6.8(c) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Equity Participant.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property (personal or real, tangible or intangible) and stamp taxes), levies, imposts, duties, charges, assessments or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon.

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by

Section 10(b)(3)(xvii) of the Participant Agreement and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed (or ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement) by an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Emerson Finance Co. and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred

by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp, APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale; (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common facilities); (xiii) simulator; and (xiv) oil and diesel fuel inventories; (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements; and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii) railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

Appendix B
to
Participation Agreement

BILL OF SALE AND ASSIGNMENT

BILL OF SALE AND ASSIGNMENT

dated as of _____, 19__

from

[EMERSON FINANCE CO.]

to

ARIZONA PUBLIC SERVICE COMPANY

BILL OF SALE AND ASSIGNMENT, dated as of _____, 19__, from [EMERSON FINANCE CO.], a [Delaware] corporation (the Equity Participant), to ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (APS).

W I T N E S S E T H:

WHEREAS, pursuant to Section 7(b)(4) of the Participation Agreement dated as of August 1, 1986 among the Equity Participant, PVNGS Funding Corp., Inc., Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants, The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee and APS, as Lessee (the Participation Agreement), the Equity Participant desires to sell and APS desires to buy the Assigned Property (as hereinafter defined);

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.01. Definitions. For purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in the Participation Agreement.

ARTICLE II

ASSIGNMENT OF TRUST ESTATE

SECTION 2.01. Assignment. Equity Participant does hereby grant, bargain, convey, sell, assign, transfer and set over to APS, on an as is, where is basis, free and clear of Equity Participant's Liens but otherwise without recourse, representation or warranty, express or implied, of any nature whatsoever, all Equity Participant's right, title and interest in, to and under the Trust Estate except Excepted Rights and the Equity Participant's right to receive Excepted Payments (the Assigned Property) [, subject to Equity Participant's

security interest in, and general lien upon, all the right, title, and interest of APS, as successor Equity Participant, in, to and under the Assigned Property*]. The disclaimer of representations and warranties set forth in the second sentence of Section 6(b) of the Facility Lease is hereby incorporated herein as fully as if set forth at this place. [Notwithstanding the foregoing transfer and assignment of the Assigned Property to APS, the obligation of APS to make the payments provided in Section [insert applicable section: 9(c), 9(d) or 16(e)] of the Facility Lease (together with interest thereon in accordance with Section 3(b) of the Facility Lease) (or to make other payments in a like amount) shall not be deemed to be canceled or discharged but shall continue until all such amounts are so received by Equity Participant pursuant to the provisions of Section 7(b)(4) of the Participation Agreement.*] [The Equity Participant hereby acknowledges receipt of \$_____ representing payment in full of all amounts due to the Equity Participant under Section [insert applicable section: 9(c), 9(d) or 16(e)] of the Facility Lease.**]

ARTICLE III

EFFECTIVENESS OF TRANSFER

SECTION 3.01. Effectiveness of Transfer. The transfer of the Assigned Property shall become effective without further action upon the execution and delivery by the Equity Participant to APS of this Bill of Sale and Assignment and the furnishing of a counterpart of this Bill of Sale and Assignment to the Owner Trustee.

* To be inserted if on the date of the transfer the Equity Participant has not received the payments provided for in Section 9(c), 9(d) or 16(e) of the Facility Lease, as the case may be.

** To be inserted if on the date of the transfer the Equity Participant has received the payments provided for in Section 9(c), 9(d) or 16(e) of the Facility Lease, as the case may be.

ARTICLE IV

MISCELLANEOUS

SECTION 4.01. Successors and Assigns. This Bill of Sale and Assignment shall be binding upon the Equity Participant and its successors and shall inure to the benefit of APS and its successors and assigns.

SECTION 4.02. Governing Law. This Bill of Sale and Assignment shall be governed by and construed and enforced in accordance with the law of the State of New York.

IN WITNESS WHEREOF, the undersigned has caused this Bill of Sale and Assignment to be duly executed as of the day and year written above.

[EMERSON FINANCE CO.]

By _____
Title:

APPENDIX C
to
PARTICIPATION AGREEMENT

SECTION 48(d) ELECTION

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended (the Code), and sections 1.48-4(f) and 1.1502-77(a) of the Income Tax Regulations promulgated under the Code (the Regulations), EMERSON FINANCE CO., a Delaware corporation (the Equity Participant), as beneficiary of a trust created by a Trust Agreement, dated as of August 1, 1986, between the Equity Participant and THE FIRST NATIONAL BANK OF BOSTON, as Owner Trustee (the Owner Trustee or the Lessor), _____, a _____ corporation as the common parent of affiliated group of corporations of which Equity Participant is a member (the Common Parent) and the Owner Trustee, hereby elect to treat ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), as lessee under a Facility Lease, dated as of August 1, 1986 (the Facility Lease), between the Owner Trustee, as Lessor, and APS, as Lessee, as having acquired the property described below for purposes of the credit allowed by sections 38 and 46(a)(1) of the Code.

(i) The name, address and taxpayer account number of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are as follows:

(a) Emerson Finance Co., 111 East Prospect, Stamford, CT 06904, Attention: President. Taxpayer account number: [TAX I.D. No.].

(b) Common Parent.

(c) The First National Bank of Boston, as Owner Trustee, 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate Trust Division. Taxpayer account number:

(d) Arizona Public Service Company, 411
North Central Avenue, Phoenix, Arizona 85004.
Taxpayer account number [TAX I.D. No.].

(ii) The district director's offices with which the income tax returns of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are filed are as follows:

(a) Emerson Finance Co.: [DISTRICT DIRECTOR/OP].

(b) Common Parent.

(c) First National Bank of Boston, as Owner Trustee:

(d) Arizona Public Service Company:
[DISTRICT DIRECTOR/LESSEE].

(iii) The property with respect to which the election is being made is an undivided interest in Palo Verde Nuclear Generating Station, Unit 2, having a fair market value of [MKT. VALUE/UNDIVIDED INTEREST].

(iv) The date on which possession of the property is transferred to the Lessee is August 18, 1986.

(v) The property is "10-year property" within the meaning of section 168(c)(2)(C) of the Code, and the estimated useful life category of the property in the hands of the Lessor is seven years or more.

(vi) Pursuant to section 48(d)(1)(A) of the Code and section 1.48-4(c)(2)(i) of the Regulations, the Lessee is treated as having acquired the leased property for an amount equal to the fair market value of property on the date possession is transferred to the Lessee.

(vii) Neither the Equity Participant, the Common Parent nor the Owner Trustee is itself a lessee with respect to the property.

EMERSON FINANCE CO.

By _____
Val Sharp,
President

THE FIRST NATIONAL BANK OF
BOSTON, as Owner Trustee

By _____
Martin P. Henry
Assistant Vice President

Date: August 18, 1986

[COMMON PARENT]

By _____

CONSENT TO ELECTION

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended, and sections 1.48-4(f)(1) and 1.48-4(h) of the Income Tax Regulations promulgated thereunder, ARIZONA PUBLIC SERVICE COMPANY, as Lessee under the Facility Lease described within, hereby consents to the foregoing Section 48(d) Election.

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Paul A. Williams II,
Vice President and Treasurer

Date: August 18, 1986

APPENDIX D
to
PARTICIPATION AGREEMENT

SUMMARY STATEMENT
under
SECTION 48(d)

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended (the Code), and section 1.48-4(j) of the Income Tax Regulations promulgated thereunder, EMERSON FINANCE CO., a Delaware corporation (the Equity Participant), as beneficiary of a trust created by a Trust Agreement, dated as of August 1, 1986, between the Equity Participant and THE FIRST NATIONAL BANK OF BOSTON, as Owner Trustee (the Owner Trustee or the Lessor), _____, a _____ corporation, as the common parent of an affiliated group of corporations of which the Equity Participant is a member (the Common Parent), and the Owner Trustee, hereby make this Summary Statement with respect to their election to treat ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), as lessee under a Facility Lease, dated as of August 1, 1986, between the Owner Trustee, as Lessor, and APS, as Lessee, as having acquired the property described below for purposes of the credit allowed by sections 38 and 46(a)(1) of the Code.

(i) The name, address and taxpayer account number of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are as follows:

(a) Emerson Finance Co., 111 East Prospect, Stamford, CT 06904, Attention: President. Taxpayer account number: [TAX I.D. No.].

(b) Common Parent.

(c) The First National Bank of Boston, as Owner Trustee, 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate Trust Division. Taxpayer account number: .

(d) Arizona Public Service Company, 411
North Central Avenue, Phoenix, Arizona 85004.
Taxpayer account number [TAX I.D. No.].

(ii) The property to which this Summary Statement is made is an undivided interest in Palo Verde Nuclear Generating Station, Unit 2, having a fair market value of \$200,000,000. The property is "10-year property" within the meaning of section 168(c)(2)(C) of the Code, and the estimated useful life category of the property in the hands of the Lessor is seven years or more.

ANNEX A

1. The effectiveness of Section 6.11 of the Indenture is suspended in its entirety and the following provisions shall apply in lieu thereof:

Except as otherwise provided in this Section, but notwithstanding any contrary or inconsistent provision of the Indenture, subject, however, to Section 10.2 of the Indenture, (a) at all times prior to the occurrence of an Indenture Event of Default, the Owner Trustee shall retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree or consent to any amendment to, or any waiver, discharge or termination of, or give any consent under any term or provision of Sections 2(c), 3(g), 4, 7, 8(f) (iv), 9(i), 11, 15(i) (x), (i) (y), (vii) and (x) and the provisions relating to the redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease; and, provided, further, that the Owner Trustee shall, in any event, observe and perform its covenants contained in clause (iv) of Section 6.1 of the Indenture; and, provided, further, that during the continuance of any Event of Default the Owner Trustee shall promptly provide the Indenture Trustee with notice or copies of any notice, consent, waiver or approval given or received and any other action taken under clause (a); (b) upon and for a period not to exceed 60 days after the occurrence of an Indenture Event of Default described in clause (y) of paragraph (a) of Section 6.3 of the Indenture, (i) the Owner Trustee and the Agent shall consult and cooperate in good faith, and, the Owner Trustee and the Indenture Trustee shall act or refrain from acting concurrently, in exercising all rights, powers and remedies of each arising under the Facility Lease and the Indenture, respectively, in all instances with a view to protecting and preserving the respective rights and remedies of the Owner Trustee and

the Holders of the Notes under the Facility Lease and the Indenture and, to the extent reasonably practicable, maximizing the prospects of recovery; without limiting the generality of the foregoing, the Owner Trustee and Indenture Trustee shall jointly exercise all rights enumerated in clause (a) above; (c) upon and at all times after the occurrence of an Indenture Event of Default described in clause (x) (ii) of paragraph (a) of Section 6.3 of the Indenture or under the circumstances described in clause (x) (i) of such paragraph, the Indenture Trustee shall have, and may freely exercise, to the exclusion of the Owner Trustee, all rights enumerated in clause (a) above and under the Indenture; provided however, that nothing in this Section shall be deemed or construed to require the Owner Trustee or Indenture Trustee to act or refrain from acting in violation of Applicable Law, nor shall the exercise of any rights, powers and remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee as defined in the ANPP Participation Agreement. Notwithstanding any provision of this Section to the contrary (other than the proviso to the preceding sentence), the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the "Stated Price") and (iii) Owner Trustee shall not have notified the Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date within 60 days after the date of such notice of election. If the Owner Trustee shall fail timely to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate to any Person (other than the Indenture Trustee, Agent or any Holder(s) or Affiliates of any thereof) at a price no lower than the Stated Price at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the Stated Price, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all of the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate. At any time after the

termination of the Facility Lease or expiration of the 180 day period described in the second preceding sentence, the Indenture Trustee may exercise any right under Applicable Law to dispose of any interest in the Lease Indenture Estate, free of any right of the Owner Trustee to purchase the same.

2. Notwithstanding anything to the contrary contained in Section 6.8(c) of the Indenture, the Owner Trustee shall not terminate the Facility Lease or arrange for the substitution of another Person as lessee under a new lease without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

3. Notwithstanding anything to the contrary contained in Section 2.3 of the Indenture, there shall be no release of all or any portion of the Lease Indenture Estate from the security or other interest created by Section 2.1 of the Indenture without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

4. If at the time any Special Transfer is effected, the Lessee shall not have assumed the obligations under the Initial Series Notes, any subsequent breach by Lessee of its covenants contained in Section 10(b)(3)(vii) of the Participation Agreement shall be an event of Default and an Indenture Event of Default.

5. Any failure by the Owner Trustee to pay the Initial Series Notes in full when and as required by Section 13(d) or Section 14(b) or 14(c) shall be an Indenture Event of Default.

6. The provisions of this Annex A shall prevail to the extent they are inconsistent with or contrary to the provisions of any of the Transaction Documents.

7. The provisions of this Annex A shall remain in full force and effect until the full payment of all principal of and premium, if any, and interest on the Initial Series Notes.

AMENDMENT NO. 1

dated as of November 1, 1986

to

PARTICIPATION AGREEMENT

dated as of August 1, 1986

among

EMERSON CAPITAL CORPORATION
(assignee of EMERSON FINANCE CO.),
as Equity Participant

BANK OF AMERICA
NATIONAL TRUST AND SAVING ASSOCIATION,
for itself and as Agent for the Original
Loan Participants under the Bank Agency
Agreement, as Agent

PVNGS FUNDING CORP., INC.,
as Funding Corporation

THE FIRST NATIONAL BANK OF BOSTON,
in its individual capacity and as Owner Trustee
under a Trust Agreement,
dated as of August 1, 1986,
with the Equity Participant, as Owner Trustee

CHEMICAL BANK,
in its individual capacity and as Indenture Trustee
under a Trust Indenture, Mortgage, Security Agreement
and Assignment of Facility Lease, dated as of
August 1, 1986,
with the Owner Trustee, as Indenture Trustee

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

AMENDMENT NO. 1, dated as of November 1, 1986, to the Participation Agreement, dated as of August 1, 1986, among EMERSON CAPITAL CORPORATION, a Delaware corporation, as a assignee of Emerson Finance Co. (the Equity Participant), BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, for itself (Bank of America) and as agent for the Original Loan Participants (the Agent), PVNGS FUNDING CORP., INC., a Delaware corporation (Funding Corp.), THE FIRST NATIONAL BANK OF BOSTON, a national banking association, in its individual capacity (FNB) and as Owner Trustee (the Owner Trustee) under a Trust Agreement, dated as of August 1, 1986, with the Equity Participant, CHEMICAL BANK, a New York banking corporation, in its individual capacity (Chemical) and as Indenture Trustee (the Indenture Trustee) under a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, with the Owner Trustee, and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee).

W I T N E S S E T H :

WHEREAS, the Equity Participant, the Agent, Funding Corp., the Owner Trustee, the Indenture Trustee and the Lessee have previously entered into a Participation Agreement dated as of August 1, 1986 (the Participation Agreement);

WHEREAS, the Initial Series Notes were issued by the Owner Trustee in connection with the acquisition of the Undivided Interest and the Real Property Interest;

WHEREAS, Section 2(d) of the Participation Agreement provides for a refunding of the Initial Series Notes upon the satisfaction of the conditions set forth in Sections 2(d), 2(e) and 11(c) of the Participation Agreement;

WHEREAS, Section 3(d) of the Facility Lease provides for an adjustment to Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event of a Change in Tax Law;

WHEREAS, the parties hereto wish to refund the Initial Series Notes;

WHEREAS, such refunding of the Initial Series Notes necessitates this Amendment No. 1 to Participation Agreement (Amendment No. 1);

WHEREAS, Section 10.1(viii) of the Indenture provides, among other things, that the Owner Trustee and Indenture Trustee may, without consent of the Holders of Notes Outstanding, execute a supplement to the Indenture in order to evidence the issuance of and to provide the terms of Additional Notes;

WHEREAS, the Owner Trustee and the Indenture Trustee intend to execute Supplemental Indenture No. 1, dated as of November 1, 1986 (Supplemental Indenture No. 1), to the Indenture, providing for the issuance under the Indenture of the Refunding Notes (as defined in Supplemental Indenture No. 1) and amending certain provisions thereof and Appendix A thereto;

WHEREAS, Section 10.2(ii) of the Indenture provides, among other things, that, upon receipt of a written instruction from the Lessee and the Owner Trustee, the Indenture Trustee shall consent to certain amendments to the Facility Lease and the Assignment and Assumption;

WHEREAS, the Owner Trustee and the Lessee intend to execute Amendment No. 1, dated as of November 1, 1986 (Lease Amendment No. 1), to the Facility Lease, to amend certain provisions thereof, Appendix A thereto and certain schedules thereto; and

WHEREAS, the Owner Trustee and the Lessee intend to execute Amendment No. 1, dated as of November 1, 1986 (Assignment and Assumption Amendment No. 1), to the Assignment and Assumption, to amend Appendix A thereto;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

Except as otherwise defined herein and in the recitals, capitalized terms used herein shall have the respective meanings set forth in Appendix A to the Participation Agreement.

SECTION 2. Agreement of Funding Corp.

Subject to the terms and conditions hereof and of Sections 2(d), 2(e) and 11(c) of the Participation Agreement, on the Refunding Date, Funding Corp. shall make a Refunding Loan and a Releveraging Loan to the Owner Trustee by paying to the Indenture Trustee immediately available funds in an amount equal to \$160,000,000.

SECTION 3. Issuance of Refunding Notes by Owner Trustee; Application of Proceeds.

Subject to the terms and conditions hereof and of Sections 2(d), 2(e) and 11(c) of the Participation Agreement and Section 3.5 of the Indenture, on the Refunding Date, upon receipt of the Refunding Loan and the Releveraging Loan to be made by Funding Corp. in accordance with Section 2 hereof, the Indenture Trustee, at the direction of the Owner Trustee, shall (a) authenticate and deliver the Refunding Notes, in the aggregate principal amount of the Refunding Loan and the Releveraging Loan and bearing interest at the rates per annum and in the amounts, respectively, set forth in, or determinable under, the Indenture, (b) apply the proceeds of the Refunding Loan to the prepayment in full of the principal of the Initial Series Notes and (c) apply the proceeds of the Releveraging Loan to pay the partial repayment of the investment originally made by the Equity Participant pursuant to Section 3 of the Participation Agreement. Notwithstanding any provision of the Participation Agreement or the Facility Lease to the contrary, it is understood and agreed that additional adjustments pursuant to Section 3(d) of the Facility Lease may be made at one time during the year commencing November 20, 1986 and no more frequently than annually thereafter.

SECTION 4. Implementation.

(a) Forms. The forms of Supplemental Indenture No. 1, Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 are attached hereto as Exhibits A, B and C, respectively.

(b) Request by the Equity Participant. In accordance with Section 2.01 of the Trust Agreement, the Equity Participant hereby requests that the Owner Trustee (i) execute and deliver this Amendment No. 1,

Supplemental Indenture No. 1, Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 (collectively, the Refunding Amendments), (ii) execute the Refunding Notes and request the Indenture Trustee to authenticate and deliver the Refunding Notes pursuant to Section 3.5(2) of the Indenture and (iii) execute and deliver all other agreements, instruments and certificates contemplated by the Transaction Documents, the Financing Documents and the Refunding Amendments.

(c) Instruction and Consent. In accordance with Section 10.2 of the Indenture, the Lessee and the Owner Trustee hereby instruct the Indenture Trustee to consent to Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 and the Indenture Trustee so consents. In accordance with Section 10.1 of the Indenture, the Owner Trustee and the Indenture Trustee hereby consent and agree to execute Supplemental Indenture No. 1.

(d) Recordations and Filings. The Lessee agrees that it will cause to be made the recordations and filings set forth in Schedule 1 hereto and that such filings and recordations are all the recordations and filings that are necessary in order to preserve, protect and perfect the Owner Trustee's rights and interests under the Facility Lease, as amended by Lease Amendment No. 1, and the first and prior security interest of the Indenture Trustee in the Lease Indenture Estate under the Indenture, as amended by Supplemental Indenture No. 1.

SECTION 5. Conditions Precedent.

(a) Conditions Precedent to Obligations of Funding Corp. The obligations of Funding Corp. to take the actions specified in Section 2 with respect to the Owner Trustee on the Refunding Date shall be subject to the following conditions precedent:

(i) each of the Underwriting Agreement dated November 6, 1986 (the "Underwriting Agreement") and the Terms Agreement dated November 6, 1986 (the "Terms Agreement") among Funding Corp., the Lessee, and The First Boston Corporation, Kidder, Peabody & Co. Incorporated and Salomon Brothers Inc, individually and as representatives of the several underwriters identified therein

(collectively, the "Underwriters") relating to the offer and sale to the public of \$273,000,000 aggregate principal amount of Secured Lease Obligation Bonds Series 1986 of Funding Corp. (the "Bonds") shall have been executed and delivered;

(ii) the Underwriters shall have purchased the Bonds pursuant to, and in accordance with the terms of, the Underwriting Agreement and the Terms Agreement;

(iii) there shall have been delivered to Funding Corp., the Indenture Trustee and the Lessee copies of the opinions delivered to the Underwriters pursuant to Sections 5(d), 5(e), 5(f) and 5(g) of the Underwriting Agreement; and

(iv) the conditions of the obligations of the Underwriters set forth in Sections 5(a), 5(b), 5(c), 5(d), 5(e), 5(f), 5(g), 5(i) and 5(j) of the Underwriting Agreement shall have been met.

(b) Conditions Precedent to Obligations of the Owner Trustee. The obligations of the Owner Trustee to issue and deliver the Refunding Notes to Funding Corp. on the Refunding Date in consideration of the Refunding Loan and the Releveraging Loan shall be subject to performance by Funding Corp. of its obligations under Section 2 hereof.

(c) Conditions Precedent to Obligations of the Indenture Trustee. The obligations of the Indenture Trustee to take the action required by Section 3 hereof on the Refunding Date shall be subject to fulfillment of the conditions set forth in Section 3.5 of the Indenture.

SECTION 6. Amendments.

(a) Section 8(c)(5) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in clause (ii) of Section 8(c)(5).

(b) Section 10(a)(5) of the Participation Agreement is amended hereby by adding the phrase "and

the Real Property Interest" after the phrase "Undivided Interest" in clause (vi) of Section 10(a)(5).

(c) Section 10(a)(6) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the second use of the phrase "Undivided Interest" in Section 10(a)(6).

(d) Section 10(b)(3)(ii)(A) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 10(b)(3)(ii)(A).

(e) Section 10(b)(3)(viii) of the Participation Agreement is amended in its entirety as follows:

"(viii) Decommissioning. (A) Unit 2, the Common Facilities used in respect of Unit 2, the other property included in the Unit 2 Retained Assets and allocable to Unit 2 and the portion of the PVNGS Site allocable to Unit 2 shall be decommissioned and retired from commercial service in accordance with Applicable Law and, to the extent a method of decommissioning is not prescribed by Applicable Law, by the method for decommissioning determined as provided in the ANPP Participation Agreement (the foregoing being herein referred to as Decommissioning). (B) As between the Lessee, the Owner Trustee, the Equity Participant, each Loan Participant and any transferee (including by way of lease) or assignee of any of the Lessor's or the Equity Participant's right, title or interest in Unit 2 (all such Persons being herein referred to as Decommissioning Beneficiaries), the Lessee agrees to pay, be solely responsible for, and to indemnify such parties against, all costs and expenses relating or allocable to, or incurred in connection with, Decommissioning (but, in the case of any such transferee or assignee who becomes a "Participant", as defined in the ANPP Participation Agreement, only to the extent of the Unit 2 Interest) (all such costs and expenses, to the extent of a 29.1% interest in Unit 2, being herein referred to as Decommissioning Cost), notwithstanding (i) the

occurrence of the Lease Termination Date, any Default, Event of Default, Event of Loss, Deemed Loss Event or any other event or occurrence, (ii) any provision of any Transaction Document, or other document, instrument or agreement, including the ANPP Participation Agreement, (iii) any provision of the License or any other license or permit, or (iv) any Applicable Law, either now or hereafter in effect, charter or by-law provision, Governmental Action or other impediment, including, without limitation, the bankruptcy or insolvency of the Lessee; it being understood that (x) the obligations of the Lessee under this clause (B) are and shall be absolute, unconditional and irrevocable and (y) the obligations of the Lessee under this clause (B) shall not extend to any interest of any Decommissioning Beneficiary acquired other than as a Decommissioning Beneficiary hereunder. Insofar as the obligations of the Lessee under this clause (B) relate to the portion of Unit 2 in excess of the Unit 2 Interest the Lessee shall be subrogated to the rights, if any, of the Decommissioning Beneficiaries against other Persons in respect of such portion of Decommissioning, provided that the Lessee shall not exercise any right to which it has been subrogated in any manner materially adverse to the Decommissioning Beneficiaries. (C) The Lessee shall use its best efforts to cause the ANPP Administrative Committee to use the safest and most reliable method of Decommissioning consistent with public health and safety. (D) The Lessee shall establish a special decommissioning trust fund or funds (the Decommissioning Trust Fund) for the accumulation and full funding of amounts sufficient by December 31, 2015 to pay Decommissioning Cost. For this purpose, Decommissioning Cost shall be as determined by an expert selected by the Equity Participant and reasonably acceptable to the Lessee (the Decommissioning Expert). For purposes of making such determination, such expert shall assume that the method of Decommissioning Unit 2 shall be the costlier of (i) the DECON method of decommissioning (if not prohibited by Applicable Law), plus cost of removal, or

(ii) the method of decommissioning required under Applicable Law. The Decommissioning Trust Fund shall be created as promptly as practicable after the Closing Date by the execution and delivery of the Decommissioning Trust Agreement. The Decommissioning Trust Fund shall be funded by the making of semi-annual deposits in the Decommissioning Trust Fund (with the first such semi-annual deposit to be made on or before the fifth anniversary of the Closing Date) by the Lessee in such amounts as would, based on investments in such securities as are permitted under the Decommissioning Trust Agreement and utilizing the actuarial assumptions used by the Lessee as of the Closing Date for its pension fund, as such assumptions may be changed from time to time by the Lessee with the consent of the Equity Participant, result in the Decommissioning Trust Fund being funded by December 31, 2015 in the full amount of the Decommissioning Cost; provided, however, that such actuarial assumptions shall reflect that earnings on amounts deposited in the Decommissioning Trust Fund shall be subject to Federal income taxation until such time that under Applicable Law such earnings on such amounts will not be subject to Federal income taxation. During the first 25 years after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert every five years. Commencing in the 26th year after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert each year. Immediately following each such determination by the Decommissioning Expert prior to December 31, 2015, the Lessee will make appropriate adjustments, if required, in its semi-annual deposits to be made thereafter so that, based on the investment and actuarial assumptions then in effect with respect to the Decommissioning Trust Fund, such Fund will be funded in the full amount of the Decommissioning Cost as so determined by December 31, 2015. During the first 20 years following the Closing Date, the Decommissioning Trust Fund will be invested and reinvested in accordance with standards no more liberal than the investment guidelines

and actuarial assumptions set forth in the Decommissioning Trust Agreement. Commencing in the 21st year following the Closing Date and thereafter, the Decommissioning Trust Fund will be invested and reinvested in Decommissioning Fund Permitted Investments; provided, however, that in no event shall the Decommissioning Trust Fund be invested in any securities of the Lessee or any Affiliate thereof. The Decommissioning Trust Fund shall be the fund of the Lessee, provided that the Lessor shall be granted and shall have a security interest in such fund as security for the obligations of the Lessee under this Section 10(b)(3)(viii). If, after the Decommissioning of Unit 2, there shall be any funds remaining in the Decommissioning Trust Fund, such funds shall be the property of, and be paid to, the Lessee. (E) In the event that (i) the Facility Lease shall have expired or terminated on or after December 31, 2015, (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default) and (ii) thereafter the Lessor shall (1) release the Undivided Interest to any Person or (2) retain the Undivided Interest and sell power and energy from its Generation Entitlement Share, then after the Lessor has received (x) in the case of clause (1) above, net rents (after reduction for expenses incurred by the Lessor in connection therewith) in an aggregate amount (when discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) equal to 23.5% of Facility Cost, as adjusted to reflect inflation or deflation from the Closing Date to the time of determination (the Adjusted Base Amount), or (y) in the case of clause (2) above, net electric revenues (after reduction for expenses incurred by the Lessor in earning such revenues) in an aggregate amount (discounted as aforesaid) equal to the Adjusted Base Amount, the Lessor shall thereafter reimburse the Lessee out of any further net rent received or net proceeds received from the sale of power and energy to the extent that such rent or proceeds are attributable to the decommissioning obligation

o f t h e L e s s e e u n d e r t h i s
Section 10(b)(3)(viii) with respect to the
period from and after the Lease Termination
Date through the remaining economic useful
life of Unit 2 (payable on an annual basis
with respect to each year or portion thereof
during the term of such lease referred to in
clause (1) above or such period referred to in
clause (2) above during which the Lessor
retains the Undivided Interest); provided,
however, that when such amount has been paid
the Lessor shall have no further obligation to
make reimbursement to the Lessee pursuant to
this Section 10(b)(3)(viii). (F) In the event
that (i) the Facility Lease shall have expired
or terminated on or after December 31, 2015
(other than in connection with an Event of
Loss, Deemed Loss Event or Event of Default),
(ii) the Lessor shall sell the Undivided
Interest to any Person (including the Lessee
in connection with the exercise by the Lessee
of the purchase option provided by
Section 13(c) of the Facility Lease), and
(iii) the net sales proceeds (discounted back
to the Lease Termination Date at a rate per
annum equal to the Prime Rate as of the Lease
Termination Date) received by the Lessor in
connection therewith shall exceed the Adjusted
Base Amount (reduced by the net amounts, if
any, actually realized by the Lessor pursuant
to clause (E) above), then the Lessor shall
reimburse the Lessee out of the net proceeds
of such sale, to the extent that such proceeds
are attributable to the decommissioning obli-
gation of the Lessee under this
Section 10(b)(3)(viii) with respect to the
period from and after the Lease Termination
Date through the remaining economic useful
life of Unit 2, whereupon the reimbursement
obligation of the Lessor under this
Section 10(b)(3)(viii) shall terminate;
provided, however, that any such reimbursement
shall not reduce the amount of such net sales
proceeds retained by the Lessor to an amount
(discounted as aforesaid) equal to less than
the Adjusted Base Amount (reduced by the net
amounts, if any, actually realized by the
Lessor pursuant to clause (E) above). The
reimbursement obligations of the Lessor under

clauses (E) and (F) of this Section 10(b)(3)(viii) are for the the sole benefit of the Lessee, and no other Person shall be a third party beneficiary with respect thereto. For purposes of this Section 10(b)(3)(viii), (x) the amount of net rents, net revenues and net sales proceeds attributable to the decommissioning obligation of the Lessee shall be the amount by which such rents, revenues and proceeds are greater than they would have been if the Lessee had had no such obligation, and (y) the amount thereof attributable to the period after the Lease Termination Date shall be the amount determined in the immediately preceding clause (x) multiplied by a fraction the denominator of which is the number of months in the period commencing May 20, 1986, and ending on the expiration of the economic useful life of Unit 2 as estimated at the time a determination is being made pursuant to this Section 10(b)(3)(viii) and the numerator of which is the number of months in the period commencing on the Lease Termination Date and ending on the expiration of such economic useful life. In the event that the Lessee and the Lessor shall not agree as to the amount of net rents, net electric revenues or net sales proceeds attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date, such amount shall be determined by the Appraisal Procedure. (G) Upon presentation of evidence by the Lessee, reasonably satisfactory to the Equity Participant and the Owner Trustee, that there are amounts then due to pay Decommissioning Cost, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to be delivered pursuant to the Decommissioning Trust Agreement for payment of Decommissioning Cost. (H) Upon presentation of a certificate of a nuclear expert selected by the Lessee and reasonably satisfactory to the Equity Participant and the Owner Trustee, stating that Decommissioning has been completed and all costs and expenses relating or allocable to, or incurred in connection

with, Decommissioning have been paid in full, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to release any funds then remaining in the Decommissioning Trust Fund. (I) Notwithstanding anything in this Participation Agreement or any other Transaction Document to the contrary, the Equity Participant, the Owner Trustee and the Lessee agree to cooperate in amending this Participation Agreement and the Decommissioning Trust Agreement to the extent necessary to enable the Decommissioning Trust Agreement to comply with Section 468A of the Code, or to establish a separate fund meeting the requirements of said Section 468A; provided, however, that in no event shall any such amendment have a material adverse effect on the Equity Participant's rights in Unit 2 or its security interest in the Decommissioning Trust Fund."

(f) Section 14(a) of the Participation Agreement is amended hereby (i) by adding the phrase "and the last sentence of Section 3(b)" after the phrase "this Section 14" in both places where it appears, (ii) by adding the phrase "the law firms referred to in clause (i) above," before the phrase "White & Case" in clause (v) of Section 14(a) and (iii) by replacing the last paragraph of Section 14(a) in its entirety as follows:

"To the extent not included in Closing Date Transaction Expenses which are disbursed as provided in Section 4(a)(ii), the Owner Trustee shall pay or shall cause others to be reimbursed for, in each case with funds provided by the Equity Participant, an appropriate portion of Transaction Expenses."

(g) Section 14(b)(ii) of the Participation Agreement is amended hereby by deleting the phrase "including, without limitation, legal and other professional fees and expenses incurred by Agent" and by adding the word "Agent," before the phrase "the Loan Participants".

(h) Section 17(a) of the Participation Agreement is amended hereby by adding the phrase "and

related definitions" before the period at the end of the second sentence of Section 17(a).

(i) Since the parties to the Participation Agreement are, by executing this Amendment No. 1 and Lease Amendment No. 1, complying with Sections 19(k) and 19(l) of the Participation Agreement, those sections are hereby deleted.

(j) Appendix A to the Participation Agreement is hereby deleted in its entirety and replaced with Appendix A hereto.

SECTION 7. Miscellaneous.

(a) Execution. This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Governing Law. This Amendment No. 1 has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the law of the State of New York.

(c) Responsibility For Recitals. The recitals contained herein shall be taken as the statements of the Lessee, and the other parties hereto assume no responsibility for the correctness of the same.

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to the Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.

EMERSON CAPITAL CORPORATION

By Val Sharp
President

Date: November 19, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Original
Loan Participants

By _____
Title:

By _____
Assistant Vice President

Date: November , 1986

PVNGS FUNDING CORP, INC.

By _____
Vice President

Date: November , 1986

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to the Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.

EMERSON CAPITAL CORPORATION

By _____
President

Date: November , 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Original
Loan Participants

By 
Title: Group Vice President

By 
Assistant Vice President

Date: November 19, 1986

PVNGS FUNDING CORP, INC.

By 
Vice President

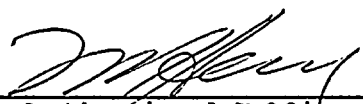
Date: November 19, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By 
Vice President and Treasurer

Date: November 19, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner
Trustee

By: 
Authorized Officer
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK, in its indi-
vidual capacity and as
Indenture Trustee

By 
Vice President

Date: November 19, 1986

Schedule 1
to
Amendment No. 1
to
Participation Agreement

RECORDATIONS AND FILINGS

Part I. Recordations in Respect to the Sale of, and Owner Trustee's Title to, the Undivided Interest and the Real Property Interest.

County Recorder, Maricopa County, Arizona:

- (i) Lease Amendment No. 1;
- (ii) Supplemental Indenture No. 1 to the Indenture; and
- (iii) Assignment and Assumption Amendment No. 1.

Part II. Filings UCC-2 Financing Statements.

(a) Separate financing statement amendments naming Arizona Public Service Company, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, with respect to the Facility Lease, as amended by Lease Amendment No. 1, were filed in the records of:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986 (regular and public utility filings); and
- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

(b) Separate financing statement amendments naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, and listing, as collateral covered thereby, the Lease Indenture Estate, were filed in the records of:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986; and

- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

(c) A financing statement amendment naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, and listing, as collateral covered thereby, the Lease Indenture Estate, was filed on November 19, 1986, with the Secretary of State of the Commonwealth of Massachusetts and the Boston Town Clerk.

Part III. Filings UCC-1 Financing Statements.

Financing statements naming Funding Corp., as debtor, and the Collateral Trust Trustee, as secured party, and listing, as collateral covered thereby, the "Pledged Property" under the Collateral Trust Indenture, as amended and supplemented, were filed with:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986;
and
- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof"; "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the initial series of Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Aggregate Liability shall mean the amount of Aggregate Liability for a single Nuclear Incident of all Persons Indemnified, as determined in accordance with the Price-Anderson Act.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Adjustment Factor shall mean the quotient obtained by dividing the number of Nuclear Facilities having operating licenses by 100.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive) or accrual of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

Aggregate Liability shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "aggregate liability", the term "Aggregate Liability" shall be similarly expanded.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 13(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes, as amended.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated as of August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under the Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York or Boston, Massachusetts are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement is or is not included or reflected in the plans and specifications for Unit 2, as built, and (b) any alteration, modification, addition or

improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 2 to the Facility Lease, and (ii) during any Renewal Term, the amount equal to (A) the present value (declining in semi-annual steps over such Renewal Term and discounted at a rate of 10%) of the remaining Basic Rent payable from time to time in respect of the Undivided Interest for such Renewal Term plus (B) the present value of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term (increasing in semi-annual steps over such Renewal Term and discounted at a rate of 10%) all as set forth in a schedule to be prepared prior to the commencement of such Renewal Term. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation), of

any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean the Collateral Trust Indenture dated as of November 1, 1986, among APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS facilities which are common to all generating units, including Unit 2, at PVNGS.

Common Parent shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Current Pricing Assumptions shall mean the assumptions attached to the letter from the Lessee to the Equity Participant dated November 19, 1986, as such letter may be replaced from time to time with the consent of the Equity Participant.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Expert shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deed shall mean the Deed, dated as of August 18, 1986, from APS to the Owner Trustee.

Deemed Loss Event shall mean any of the following events (unless and until waived in writing by the Equity Participant):

(1) Utility Regulation. If at any time from and including the Closing Date and before the Lease Termination Date, the Lessor or the Equity Participant, by reason of the acquisition or ownership of the Undivided Interest or the Real Property Interest or any part thereof by the Lessor (or any beneficial interest therein by the Equity Participant) or the lease of the Undivided Interest to the Lessee or any of the other transactions contemplated by the Transaction Documents, shall be deemed by any Governmental Authority having jurisdiction to be, or shall become subject to regulation (other than Non-Burdensome Regulation) as, an electric utility, a public utility or a holding company under any Applicable Law or as a consequence of any Governmental Action, and the effect thereof on the Lessor or the Equity Participant would be, in the sole judgment of the Equity Participant, acting on the advice of counsel, adverse, except that if the Lessee, at its sole cost and expense, is contesting diligently and in good faith any Governmental Action which would otherwise constitute a Deemed Loss Event under this clause (1), such Deemed Loss Event shall be deemed not to have occurred so long as in the sole judgment of the Equity Participant (i) such

contest does not involve any danger of the foreclosure, sale, forfeiture or loss of, or the creation of any Lien on, the Undivided Interest, the Real Property Interest or any part thereof or any interest therein, (ii) such contest does not adversely affect the Undivided Interest or the Real Property Interest or any part thereof or any other property, assets or rights of the Lessor or the Equity Participant or the lien of the Indenture thereon, (iii) the Lessee shall have furnished the Equity Participant with an opinion of independent counsel satisfactory to the Equity Participant to the effect that (a) there exists a reasonable basis for contesting such determination or (b) in the case of any action arising from or related to the Lessor or the Equity Participant under the Holding Company Act, it is more likely than not that the Lessee will successfully contest such determination without the need for any appeal, (iv) such determination shall be effectively stayed or withdrawn during such contest (and shall not in the sole judgment of the Equity Participant be subject to retroactive application at the conclusion of such contest) in a manner satisfactory to the Equity Participant, and the Equity Participant shall have determined in its sole judgment that such contest and the Lessor's continued ownership of the Undivided Interest and the Real Property Interest during the pendency of such contest will not adversely affect its business or the business of any of its Affiliates, and (v) the Lessee shall have indemnified the Lessor and the Equity Participant in a manner satisfactory to the Equity Participant for any liability or loss which either may incur; it being understood, however, that the term Equity Participant as used in this clause (1) does not include any Transferee who at the time of transfer is an entity which is subject to regulation as an electric utility, public utility or a holding company under Applicable Law or Governmental Action.

(2) Change in Applicable Law. Any change in, or new interpretation by a Governmental Authority having jurisdiction relating to, Applicable Law, including, without limitation, the Price-Anderson Act, the Atomic Energy Act, the Nuclear Waste Act or the regulations of the NRC, in each case as in effect on the Closing Date, as a result of which, in the opinion of independent counsel to the Equity

Participant: (i) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified is increased; (ii) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified exceeds the amount of Financial Protection required under Applicable Law and available at the time of such Nuclear Incident; (iii) (a) the amount of Primary Financial Protection required with respect to a single Nuclear Facility under Applicable Law is increased, whether or not the total amount of Financial Protection required with respect to a single Nuclear Facility is increased, or (b) the amount of Financial Protection required under Applicable Law is increased (including, but not limited to, an increase in the amount of retrospective premiums payable under the Retrospective Rating Plan) or (c) the amount of retrospective premiums payable under the Retrospective Rating Plan in any one year with respect to two or more Nuclear Incidents is increased; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. Section 140.22 or 10 C.F.R. Section 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan) shall be modified or changed in any material respect; (v) the Lessor or the Equity Participant may become liable or responsible in any capacity (including, without limitation, through assessments imposed by a Governmental Authority) for payments owed in respect of the Nuclear Waste Fund (as such term is used in Section 302 of the Nuclear Waste Act) or in respect of the handling or disposal of nuclear waste, decontamination, storage, transportation or safekeeping of radioactive or hazardous materials or any other obligation in the nature of the foregoing; (vi) the Lessor, the Equity Participant or the Lessee may be prohibited from asserting any right, protection or defense available under Applicable Law as of the Closing Date with respect to civil or criminal actions brought in connection with a Nuclear Incident (including, without limitation, through an expansion of the waiver of defenses provision under subsection 170n. of the Atomic Energy Act); (vii) there shall be expressly created a new cause of action whereby any Person who pays or will pay retrospective premiums under the Retrospective Rating Plan or other assessments required under Applicable Law may recover the amount of such

payments from the facility at which a Nuclear Incident occurs or from any Person associated with such facility; (viii) there shall be a third tier or additional level of potential or real liability (including assessments imposed by a Governmental Authority) with respect to a Nuclear Facility; (ix) there shall be any type of claim, liability or expense (other than the costs of investigating and settling claims and defending suits for damage) excluded from the limitation of liability established by the Price-Anderson Act (through modification of the definitions of "aggregate liability", "persons indemnified", "nuclear incident" or otherwise) or excluded (or the funding or payment thereof deferred) under insurance or other Financial Protection required under Applicable Law as in effect on the Closing Date, except to the extent and in the amount expressly excluded or deferred pursuant to Applicable Law as in effect on the Closing Date; or (x) the Lessor or the Equity Participant may be exposed, during the Lease Term or after the Lease Termination Date, to any other increased real or potential liability (including, without limitation, through assessments imposed by a Governmental Authority) with respect to a Nuclear Incident or otherwise relating to the operation of PVNGS or the transactions contemplated by the Participation Agreement; provided, however, that no such change shall constitute a Deemed Loss Event if and for so long as such change or interpretation meets all the conditions constituting a Safe Harbor Change. For purposes of this clause (2), the requirement or existence of insurance, retrospective premiums, indemnities (whether by the Lessee or any other Person) or other forms of Financial Protection (similar or dissimilar to the foregoing) shall not be deemed to eliminate or negate any exposure of the Lessor or the Equity Participant to real or potential increased liability.

(3) Insurance. The Lessee shall not be in compliance with Section 10 of the Facility Lease.

(4) License. Any expiration, revocation, suspension, amendment or interpretation by any Governmental Authority of the License or any other change in Applicable Law or Governmental Action, as a result of which, prior to the Lease Termination Date, either the Lessor or the Equity Participant is

or might (i) be required to be or become a licensee under the Atomic Energy Act with respect to Unit 2 or (ii) be subject to the obligations or liabilities imposed, as of the Closing Date or thereafter, on licensees under the Atomic Energy Act with respect to Unit 2 or (iii) be otherwise subject to significant regulation.

(5) Multiple Incidents. The occurrence (i) of two or more incidents (including incidents occurring outside the United States of America), in each case at any Nuclear Facility or Facilities using a Combustion Engineering pressurized water reactor nuclear steam supply system or another nuclear steam supply system of comparable design or comparable components, the failure of which Combustion Engineering pressurized water reactor nuclear steam supply system or other nuclear steam supply system of comparable design or components results in (x) a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; (y) (A) the radiation level in the containment vessel as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equaling or exceeding 1,000 rad per hour; or (B) any measure

of radioactivity in the primary coolant system exceeding by 1,000 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (z) damage to offsite property, including, without limitation, costs for decontamination, in amounts in excess of \$15,000,000; or (ii) within a five-year period of three or more incidents, of the type and severity described in subclause (i)(x), (y) or (z) above, at any Nuclear Facility or Facilities (including incidents occurring outside the United States of America).

(6) **Illegality; Exercise of Rights and Remedies.** Any change in Applicable Law or any Governmental Action the effect of which is or might be (i) to make any of the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law, (ii) to impede the exercise by the Lessor or the Equity Participant of any right or remedy under any Transaction Document relating to the assertion of claims for Rent or monetary damages, (iii) to cause the Lessor or the Equity Participant to be or become liable in any capacity in respect of Decommissioning, including, without limitation, all or any portion of the Termination Obligation (as defined in the ANPP Participation Agreement), or (iv) to constitute an assertion to the effect that (a) the exercise by the Lessor or the Equity Participant of any right (irrespective of the event giving rise to such right) under any Transaction Document would constitute impermissible control over Unit 2 or the licensees of Unit 2, other than an assertion consistent with the second sentence of Section 184 of the Atomic Energy Act and the NRC's regulations thereunder, including, without limitation, 10 C.F.R. Section 50.81, as now in effect, or (b) the acquisition or transfer of the Undivided Interest was in violation of, or otherwise contrary to, Applicable Law.

(7) **Violations.** With respect to PVNGS, the NRC shall have issued within a two-year period (x) two or more final orders involving "Severity Level I" violations or (y) three or more final orders involving "Severity Level I" or "Severity Level II" violations, as such terms are used in Supplement I to Appendix C to 10 C.F.R., Part 2, as in effect on the Closing Date (or, if such Supplement is amended or

superseded or different categories are in effect, comparable violations).

(8) Unit 1 and Unit 3 Incidents. (1) The occurrence of an event at Unit 1 or Unit 3 (such affected unit being herein in this definition referred to as the Affected Unit) as a result of which: (w) the radiation level in the top half of the containment vessel of the Affected Unit as measured by the average of two high range radiation monitors in the upper half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of the Affected Unit shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for the Affected Unit (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of the Affected Unit's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of the Affected Unit, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date; or (2) the occurrence of a Nuclear Incident at an Affected Unit as a result of which the Affected Unit ceases to operate (or if the Affected Unit is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a

result of such Nuclear Incident) for a Period of 36 consecutive months.

(9) Radiation Level. Except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 1 or 3, the radiation level in the fuel building above either such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours.

(10) Reduced Operations. Other than in consequence of a reduction in demand, Unit 2 shall have operated in any calendar year at a net capacity factor below 35% other than as a result of a shut-down to repair damage to Unit 2; provided, however, that if the NRC shall determine at any time during the Lease Term that the operation of this paragraph might impair the ability of the Lessee or the Operating Agent to comply with the terms of the License or Applicable Law or interfere with the exercise of the NRC's jurisdiction to protect the public health and safety, then this paragraph 10 shall be deemed waived.

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its

obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank (as used herein, a Letter of Credit Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Letter of Credit Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Letter of Credit Bank, or (iii) any Letter of Credit Bank whose long-term unsecured debt securities and the long-term unsecured debt securities of any parent company of such Letter of Credit Bank are rated not less than Aa3 by Moody's, other than a Letter of Credit Bank to which the Equity Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of a Letter of Credit Bank which is part of a holding company structure, the failure of such Letter of Credit Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities but eligibility under this clause (iii) shall not be available if the cost of a Letter of Credit issued by an Letter of Credit Bank otherwise qualifying under clause (i) or (ii) for a period of five years shall be greater than the cost of the prior Letter of Credit provided by an Eligible Bank qualifying under clause (i) or (ii)); provided, however, that any Letter of Credit issued by a Letter of Credit Bank that is not incorporated in the United States shall

provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Emerson Finance Co., and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended.

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean (i) all indemnity payments to which the Owner Trustee or the Equity Participant (or the respective successors, assigns, agents, officers, directors or employees of the Owner Trustee or the Equity Participant) is entitled, (ii) any

amounts payable under any Transaction Document to reimburse the Lessor or the Equity Participant (including the reasonable expenses of the Lessor or the Equity Participant incurred in connection with any such payment) for performing or complying with any of the obligations of the Lessee under and as permitted by any Transaction Document; (iii) any insurance proceeds with respect to an Event of Loss in excess of amounts then due and owing in respect of the principal of and premium, if any, and interest on all Notes Outstanding, (iv) any insurance proceeds (or payments with respect to risks self-insured) under liability policies, (v) any payments in respect of interest to the extent attributable to payments referred to in clauses (i) through (iv) above and (vi) if the Letter of Credit has been terminated or has expired, a portion of Casualty Value, Special Casualty Value or Extraordinary Casualty Value equal to the amount by which Modified Special Casualty Value exceeds the sum of all amounts drawn under the Letter of Credit.

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and all rights and interests with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank.

Extraordinary Casualty Value, as of any date, during the Basic Lease Term, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under the applicable provision, if any, of the Facility Lease or the Participation Agreement, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on

such date, together with accrued and unpaid interest on such Notes.

Extraordinary Nuclear Occurrence shall have the meaning assigned in Section 11 of the Atomic Energy Act and the related NRC regulations (10 C.F.R. § 140.84 and 140.85), as in effect as of the Closing Date.

Facility Cost shall mean the sum of the Purchase Price and the Real Estate Investment plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement, and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined

on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended.

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; (y) any order of or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period exceeding 24 months; or (z) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which: (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one

such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which: (x) the NRC declares to be an Extraordinary Nuclear Occurrence; (y) result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured

through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; or (z) result in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee, or of the Lessee and one or more other ANPP Participants, to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown in consequence of the occurrence of an event described in (A) clause (4) or (5) above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause (8) above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months.

Financial Protection shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "financial protection", the term "Financial Protection" shall be similarly expanded.

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meaning set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, shall mean the Generation Entitlement Share of APS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all siting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Group shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, each Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture, and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles, a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean the percentage set forth opposite "Lessor's Portion" on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended, (vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Aggregate Loss shall be computed and applied in respect of Unit 2, including all interests therein, and with respect to each calendar year shall mean the sum of (i) retrospective premiums, if any, payable during such year under the Retrospective Rating Plan with respect to any Nuclear Incident which shall have occurred prior to the date of such calculation, (ii) all uninsured liquidated amounts paid or payable during such year, and not covered by the Retrospective Rating Plan, in respect of Nuclear Incidents, and (iii) other known assessments and costs and an assumed

additional amount in respect of such retrospective premiums which would be payable during such year if a Nuclear Incident, or one additional Nuclear Incident, should occur in such year.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of (x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of the Fixed Rate Renewal Term) in each case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Lessor's Portion of the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and (iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Lessor's Portion of the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or December 31 in such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage.

Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions. The after-tax yield component of Net Economic Return will be adjusted upward by 0.1% for each 1% downward adjustment in marginal federal tax rates pursuant to a Change in Tax Law; provided, however, that the maximum upward adjustment due solely to such increase in the after-tax yield component will result in an increase of .20% in the present value of Rent (discounted semi-annually using a semi-annual discount rate equal to 5.075%).

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Net Worth Factor shall mean the quotient obtained by dividing (i) PVNGS Net Worth, as of December 31 of the year prior to the date of any calculation of Net Worth Factor, by (ii) PVNGS Net Worth, as of December 31, 1985; provided, however, that Net Worth Factor shall not be less than 1.0 in respect of any year prior to 1991.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the

business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest and the Real Property Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest and the Real Property Interest on or after the Lease Termination Date or (iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes and Additional Notes issued from time to time under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Facility shall mean a facility designed for producing substantial amounts of electricity and having a rated capacity of 100,000 electrical kilowatts or more.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act, as in effect as of the Closing Date; provided that if the Atomic Energy Act shall be amended to expand the definition of "nuclear incident", the term "Nuclear Incident" shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Obsolescence Redemption Date shall mean (i) if any Bonds are outstanding on the related Termination Date, the date which is 25 days after such Termination Date, or if such date is not a Business Day, the next Business Day thereafter, or (ii) if no Bonds are outstanding on such Termination Date, the Termination Date.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used.

Original Loan Participants shall mean Bank of America and each of the other banks (the Banks) listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% per annum in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs) or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participants and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee

under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest) under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

Persons Indemnified shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "person indemnified", the term "Persons Indemnified" shall be similarly expanded.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No. 85-256, 71 Stat. 576 (1957), as amended to August 18, 1986 (except as otherwise expressly provided), including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 3 to the Participation Agreement.

Primary Financial Protection shall mean Financial Protection required to be maintained by each Nuclear Facility under Applicable Law, except for such amounts required to be maintained under a Retrospective Rating Plan.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected

to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Net Worth shall mean the sum of the consolidated common stockholders equity of APS, El Paso, PNM and Southern California, and their respective successors, as shown in their most recent respective audited financial statements; provided, however, that the consolidated common stockholders equity of any such Person shall not be included in the foregoing sum after (and only after) such time as such Person is not an ANPP Participant subject to the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 4(b) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed or by the ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund the Initial Series Notes or Outstanding Bonds.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean a Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of Refunding Bonds.

Registration Statement shall mean a registration statement, including all exhibits and all documents incorporated in such Registration Statement by reference, filed with the SEC under the Securities Act in connection with the offer, issue and sale of any Refunding Bonds or Refunding Notes.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent.

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational

responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Sevéable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Retrospective Rating Plan shall mean the industry retrospective rating plan established pursuant to the Price-Anderson Act, or any successor or similar plan established under Applicable Law.

Safe Harbor Change shall mean any Substantial Amendment, and any other change which, had it been part of the first Substantial Amendment (together with all other changes since the first Substantial Amendment) would have been a Substantial Amendment, enacted after the Closing Date, if, upon the effective date of such Substantial Amendment or other change and at all times thereafter (as shall be determined from time to time):

(A) (1) the Lessor and the Equity Participant (x) shall, as a result of such Substantial Amendment, be exempt from all real and potential liability in respect of a Nuclear Incident (Nuclear Liability) both during and after the Lease Term (unless the Equity Participant or the Lessor, as the case may be, is as of the time of a Nuclear Incident a licensee with respect to Unit 2 under the Atomic Energy Act) and (y) shall have received an opinion of independent counsel to the Equity Participant to the effect that there is no reasonable basis for a court to hold either the Lessor or the Equity Participant liable for any Nuclear Liability, both during and after the Lease Term (subject to the exception described in the parenthetical clause in clause (x) above) and (2) in the opinion

of independent counsel to the Equity Participant, such Substantial Amendment meets all the conditions stated in clause (B) below; provided, however, that part (b) in subclause (i) of clause (B) shall read as follows, "(b) the product of (1) 1.75 times (2) the Net Worth Factor times (3) the product of \$6.5 billion multiplied by the Adjustment Factor***", and subclause (iii) of clause (B) shall read as follows, "Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter shall not exceed the product of (x) 1.75 times (y) .5% times (z) the product of the Net Worth Factor times \$6.5 billion ***"; provided, further, that in the event the Equity Participant is furnished with an opinion of its independent counsel stating that, because of a change in Applicable Law, there is a significant risk that the opinion described in subclause (y) of subclause (1) above is no longer valid, then this clause (A) shall cease to be applicable; or

(B) in the event clause (A) is not applicable, as a result of such Substantial Amendment, in the opinion of independent counsel to the Equity Participant: (i) Adjusted Aggregate Liability, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed (a) the amount of Financial Protection required to be maintained by each Nuclear Facility with respect to a single Nuclear Incident or (b) the product of (1) the Net Worth Factor times (2) the product of \$6.5 billion times (3) the Adjustment Factor, and if Adjusted Aggregate Liability should exceed either (a) or (b) above the Substantial Amendment shall no longer constitute a Safe Harbor Change; (ii) the amount of Primary Financial Protection available from commercial insurance underwriters on terms substantially equivalent (in the reasonable opinion of the Equity

Participant) to the terms in effect on the Closing Date under Applicable Law and required to be maintained by licensees with respect to any single Nuclear Facility shall be at least equal to the amount required under Applicable Law (which amount shall not exceed \$500 million); (iii) Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed the product of (x) .5% times (y) the Net Worth Factor times (z) \$6.5 billion, and if Maximum Aggregate Loss should exceed the foregoing product the Substantial Amendment shall no longer constitute a Safe Harbor Change; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. § 140.22, or 10 C.F.R. § 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan), as in effect on the Closing Date, shall not have been amended or modified in any material respect; (v) the NRC shall be required to fulfill payment obligations when due from a licensee liable for damage arising out of or related to a Nuclear Incident in the event that the payment obligations of such licensee in any calendar year exceed the amount payable by such licensee in respect of such Nuclear Facility in such year under the Retrospective Rating Plan; provided, however, that the NRC shall be entitled to reimbursement through the Retrospective Rating Plan as such payments are made over time; (vi) neither the Lessee nor any other Persons Indemnified will be required to waive the defense of the statute of limitations (existing under any Applicable Law) with respect to a Nuclear Incident (except an Extraordinary Nuclear Occurrence); with respect to an Extraordinary Nuclear Occurrence such defense shall be required to be waived only as to suits instituted within 30 years after the date the Extraordinary Nuclear Occurrence which is

the subject of the suit takes place and within a prescribed number of years from the date on which the claimant first knew, or reasonably could have known, of his injury or damage and the cause thereof; (vii) neither the Lessor nor the Equity Participant shall be exposed to any increased real or potential liability (including assessments imposed by a Governmental Authority) with respect to activities authorized by the Nuclear Waste Act; (viii) none of the results contemplated in subclauses (vii) and (ix) of clause (2) of the definition of Deemed Loss Event shall have occurred; (ix) neither the Lessor nor the Equity Participant shall, in the opinion of independent counsel to the Equity Participant delivered within six months of such Substantial Amendment, be exposed to any other material increase in its real or potential liability with respect to a Nuclear Incident, either before, on or after the Lease Termination Date, except for liability arising with respect to a Nuclear Incident which takes place after the Lessor or the Equity Participant, as the case may, becomes a licensee of the NRC, and (x) neither the Lessor, the Equity Participant nor the Lessee shall be prohibited from asserting any other right, protection or defense available under Applicable Law as in effect on the Closing Date other than those rights, protections and defenses which are waived pursuant to this definition of Safe Harbor Change; provided, however, that an expansion of the waiver of defenses provision of subsection 170n.(1) of the Atomic Energy Act so that such waivers are applicable with respect to an Extraordinary Nuclear Occurrence arising out of or resulting from or occurring in the course of (a) transportation of source material, byproduct material, or special nuclear material to or from any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, (b) activities undertaken by the

Secretary, including but not limited to activities related to the storage or disposal of high-level radioactive waste, or (c) the construction, possession or operation of any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, shall not be deemed to expose the Lessor, the Equity Participant or the Lessee to any increased real or potential liability.

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor, the Equity Participant and the Indenture Trustee in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Secretary shall mean the Secretary of Energy.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount equal to (A) the present value (declining in semi-annual steps over such Renewal Term and discounted at a rate of 10%) of the remaining Basic Rent payable from time to time in respect of the Undivided Interest for such Renewal Term plus (B) the present value of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term (increasing in semi-annual steps over such Renewal Term and discounted at a rate of 10%) all as set forth in a schedule to be prepared prior to the commencement of such Renewal Term. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted securities ratings.

Summary Statement shall have the meaning set forth in Section 20(b) of the Participation Agreement.

Substantial Amendment shall mean any amendment to the Price-Anderson Act or the Atomic Energy Act which would constitute a Deemed Loss Event under clause (2) of the definition of Deemed Loss Event.

Substituted Lessee shall have the meaning set forth in Section 6.8(c) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Equity Participant.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property (personal or real, tangible or intangible) and stamp taxes), levies, imposts, duties, charges, assessments or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon.

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed (or ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement) by

an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Emerson Finance Co. and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp, APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale; (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common facilities); (xiii) simulator;

and (xiv) oil and diesel fuel inventories; (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements; and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii) railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth opposite "Unit 2 Retained Assets Portion" on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

TRUST AGREEMENT
dated as of August 1, 1986

between

EMERSON FINANCE CO.
as Equity Participant

and

THE FIRST NATIONAL BANK OF BOSTON,
as Owner Trustee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

MOFO Nuclear Trust No. 2

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TRUST AGREEMENT

TRUST AGREEMENT, dated as of August 1, 1986, between Emerson Finance Co., a Delaware corporation (the Equity Participant) and THE FIRST NATIONAL BANK OF BOSTON, a national banking association (the Owner Trustee).

W I T N E S S E T H:

WHEREAS, the Equity Participant desires to acquire the Undivided Interest and the Real Property Interest through the Trust created hereby; and

WHEREAS, The First National Bank of Boston is willing to act as Owner Trustee and to accept the Trust created hereby;

NOW, THEREFORE, in consideration of the mutual agreements herein contained and other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.01. Definitions. All capitalized terms used herein and not otherwise defined herein shall have the meanings set forth in Appendix A to the Participation Agreement. References in this Agreement to articles, sections, paragraphs and clauses are to articles, sections, paragraphs and clauses of this Agreement unless otherwise indicated.

ARTICLE II

AUTHORITY TO EXECUTE AND PERFORM VARIOUS DOCUMENTS; RATIFICATION AND CONFIRMATION; DECLARATION OF TRUST BY THE OWNER TRUSTEE

SECTION 2.01. Authority To Execute and Perform Various Documents. The Equity Participant hereby authorizes and directs the Owner Trustee (i) to execute and deliver each Transaction Document to which the Owner Trustee is to be a party and to execute and issue and request the Indenture Trustee to authenticate and deliver the Initial Series Note (each such Transaction Document, including the Initial Series Note, to be in the form approved by the Equity Participant), (ii) to execute and deliver all other agreements, instruments and certificates contemplated by the documents referred to in clause (i),

(iii) to take whatever action shall be required to be taken by the Owner Trustee by the terms of, and exercise its rights and perform its duties under, each of the documents, agreements, instruments and certificates referred to in clauses (i) and (ii) above as set forth in such documents, agreements, instruments and certificates and (iv) subject to the terms of this Agreement, to take such other action in connection with the foregoing as the Equity Participant may from time to time direct.

SECTION 2.02. Ratification and Confirmation. By certificate dated August 8, 1986 (the Section 15.6.1 Certificate), the Owner Trustee confirmed the matters required to be confirmed on the part of a lessor in a sale and leaseback transaction under Section 15.6.1 of the ANPP Participation Agreement, a copy of which certificate is attached hereto as Schedule 1. The Equity Participant, by its execution and delivery of this Agreement, ratifies and confirms the execution and delivery by the Owner Trustee of the Section 15.6.1 Certificate.

SECTION 2.03. Declaration of Trust by the Owner Trustee. The Owner Trustee hereby declares that it will hold all estate, right, title and interest of the Owner Trustee in and to the Undivided Interest, the Real Property Interest, the Transaction Documents and any other property contributed by the Equity Participant, including without limitation all amounts of Rent, insurance proceeds and requisition, indemnity or other payments of any kind, but specifically excluding any Excepted Payments (collectively, the Trust Estate), upon the trusts set forth herein and for the use and benefit of the Equity Participant.

ARTICLE III

PAYMENTS

SECTION 3.01. Payments from Trust Estate Only. All payments to be made by the Owner Trustee under this Agreement shall be made only from the income and proceeds from the Trust Estate and only to the extent that the Owner Trustee shall have received income or proceeds from the Trust Estate to make such payments in accordance with the terms hereof, except as specifically provided in Section 6.01. The Equity Participant agrees that it will look solely to the income and proceeds from the Trust Estate to the extent available for payment as herein provided and that, except as specifically provided herein, the Owner Trustee shall not be liable to the Equity Participant for any amounts payable under this Agreement and shall not be subject to any liability under this Agreement.

SECTION 3.02. Method of Payment. All amounts payable to the Equity Participant pursuant to this Agreement shall be paid or

caused to be paid by the Owner Trustee to the Equity Participant, or its nominee, by crediting the amount to be distributed to the Equity Participant to an account maintained by the Equity Participant with the Owner Trustee in immediately available funds or by transferring such amount in immediately available funds to a banking institution with bank wire transfer facilities for the account of the Equity Participant, as instructed from time to time by the Equity Participant.

ARTICLE IV

DISTRIBUTIONS

SECTION 4.01. Distributions. Subject to the terms and requirements of the Transaction Documents, all payments and amounts received by or on behalf of the Owner Trustee shall be distributed forthwith upon receipt in the following order of priority: first, so much of such payment or amount as shall be required to pay or reimburse the Owner Trustee for any fees or expenses (including reasonable attorney's fees and expenses) not otherwise paid or reimbursed to the Owner Trustee as to which the Owner Trustee is entitled to be paid or reimbursed hereunder shall be retained by the Owner Trustee; and, second, the balance, if any, of such payment or amount remaining thereafter shall be distributed to the Equity Participant.

ARTICLE V

DUTIES OF THE OWNER TRUSTEE

SECTION 5.01. Notice of Certain Events. In the event the Owner Trustee shall have knowledge of any Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event, the Owner Trustee shall give prompt written notice thereof to the Equity Participant, the Lessee, the Loan Participant and the Indenture Trustee unless such Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event no longer exists before the giving of such notice. Subject to the provisions of Section 5.03, the Owner Trustee shall take or refrain from taking such action, not inconsistent with the provisions of the Transaction Documents, with respect thereto as the Equity Participant shall direct by written instruction to the Owner Trustee. If the Owner Trustee shall have given the Equity Participant written notice of any event and shall not have received written instructions as above provided within 30 days after mailing notice of such event to the Equity Participant, the Owner Trustee may, subject to the provisions of the Transaction Documents, take or refrain from taking such action, but shall be under no duty to, and shall have no liability for its failure or refusal to, take or

refrain from taking any action with respect thereto as the Owner Trustee shall deem advisable and in the best interests of the Equity Participant. For all purposes of this Agreement, in the absence of actual knowledge of an officer in the corporate trust division of the Owner Trustee, the Owner Trustee shall not be deemed to have knowledge of any Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event unless the Owner Trustee receives written notice thereof given by or on behalf of the Equity Participant, the Lessee, the Loan Participant, the Indenture Trustee or any Holder of a Note.

SECTION 5.02. Action upon Instructions. Subject to the terms of Sections 5.01 and 5.03, upon the written instructions of the Equity Participant, the Owner Trustee will take or refrain from taking such action or actions, not inconsistent with the provisions of the Transaction Documents, as may be specified in such instructions.

SECTION 5.03. Indemnification. The Owner Trustee shall not be required to take or refrain from taking any action under this Agreement or any other Transaction Document (other than the actions specified in the first sentence of Section 5.01) unless the Owner Trustee shall have been indemnified by the Lessee or, if the Owner Trustee reasonably believes such indemnity to be inadequate, by the Equity Participant, in manner and form reasonably satisfactory to the Owner Trustee, against any liability, fee, cost or expense (including reasonable attorneys' fees and expenses) which may be incurred or charged in connection therewith, other than such as may result from the willful misconduct or gross negligence of the Owner Trustee; and, if the Equity Participant shall have directed the Owner Trustee to take or refrain from taking any action under any Transaction Document, the Equity Participant agrees to furnish such indemnity by a written undertaking of indemnification and, in addition, to pay the reasonable compensation of the Owner Trustee for the services performed or to be performed by it pursuant to such direction. The Owner Trustee shall not be required to take any action under any Transaction Document if the Owner Trustee shall reasonably determine, or shall have been advised by counsel, that such action is likely to result in personal liability for which the Owner Trustee has not been and will not be adequately indemnified or is contrary to the terms hereof or of any document contemplated hereby to which the Owner Trustee is a party or is otherwise contrary to law.

SECTION 5.04. No Duties Except as Specified in Trust Agreement or Instructions. The Owner Trustee shall not have any duty or obligation to manage, control, use, make any payment in respect of, register, record, insure, inspect, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or any other part of the Trust Estate, or to otherwise take or refrain from taking any action under or in connection with any

document contemplated hereby to which the Owner Trustee is a party, except as expressly provided by the terms of this Agreement or in written instructions from the Equity Participant received pursuant to Section 5.01 or 5.02; and no implied duties or obligations shall be read into this Agreement against the Owner Trustee. The Owner Trustee nevertheless agrees that it will, in its individual capacity and at its own cost and expense, promptly take all action as may be necessary to discharge any Lessor's Liens arising by, through or under it on any part of the Trust Estate.

SECTION 5.05. No Action Except Under Specified Documents or Instructions. The Owner Trustee agrees that it will not manage, control, use, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or any other part of the Trust Estate except (i) as required by the terms of the Transaction Documents, (ii) in accordance with the powers granted to, or the authority conferred upon, the Owner Trustee pursuant to this Agreement or (iii) in accordance with the express terms hereof or with written instructions from the Equity Participant pursuant to Section 5.01 or 5.02.

SECTION 5.06. Absence of Duties. Except in accordance with written instructions furnished pursuant to Section 5.01 and 5.02, and without limitation of the generality of Section 5.04, the Owner Trustee shall not have any duty to (i) file, record or deposit any Transaction Document or any other document, or to maintain any such filing, recording or deposit or to refile, rerecord or redeposit any such document, (ii) obtain insurance on the Undivided Interest or the Real Property Interest or effect or maintain any such insurance, other than to receive and forward to the Equity Participant any notices, policies, certificates or binders furnished to the Owner Trustee pursuant to the Facility Lease, (iii) maintain Unit 2, the Undivided Interest or the Real Property Interest, (iv) pay or discharge any Tax or any Lien owing with respect to or assessed or levied against any part of the Trust Estate, except as provided in the last sentence of Section 5.04, other than to receive and forward notice of such Tax or Lien to the Equity Participant, (v) confirm, verify, investigate or inquire into the failure to receive any reports or financial statements of the Lessee, (vi) inspect Unit 2 at any time or ascertain or inquire as to the performance or observance of any of the covenants of the Lessee or any other Person under any Transaction Document with respect to the Undivided Interest, the Real Property Interest or Unit 2 or (vii) manage, control, use, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or Unit 2 or any part thereof or any other part of the Trust Estate, except as provided in Section 5.05.

ARTICLE VI

THE OWNER TRUSTEE

SECTION 6.01. Acceptance of Trust and Duties. The Owner Trustee accepts the trusts hereby created and agrees to perform the same, but only upon the terms of this Agreement. The Owner Trustee also agrees to disburse all moneys actually received by it constituting part of the Trust Estate upon the terms of this Agreement. The Owner Trustee shall not be answerable or accountable under any circumstances, except for (i) its own wilful misconduct or gross negligence, (ii) the inaccuracy of any of its representations or warranties contained in Section 6.03 or under Section 8(a) of the Participation Agreement given expressly in its individual capacity, (iii) its failure to perform obligations expressly undertaken by it in the last sentence of Section 5.04 of this Agreement or in Section 8(b) of the Participation Agreement or (iv) Taxes based on or measured by any fees, commissions or compensation received by it for acting as trustee in connection with any of the transactions contemplated by the Transaction Documents.

SECTION 6.02. Furnishing of Documents. The Owner Trustee will furnish to the Equity Participant, promptly upon receipt thereof, duplicates or copies of all reports, notices, requests, demands, opinions, certificates, financial statements and any other writings furnished to the Owner Trustee hereunder or under the Transaction Documents, unless by the express terms of any Transaction Document a copy of the same is required to be furnished by some other Person directly to the Equity Participant, or the Owner Trustee shall have determined that the same has already been furnished to the Equity Participant.

SECTION 6.03. No Representations or Warranties as to the Undivided Interest, the Real Property Interest, Unit 2 or Documents. The Owner Trustee makes (i) NO REPRESENTATION OR WARRANTY AS TO THE TITLE, VALUE, CONDITION, DESIGN, OPERATION, MERCHANTABILITY OR FITNESS FOR USE OF THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST, UNIT 2 OR ANY OTHER REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, WITH RESPECT TO THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST OR UNIT 2 WHATSOEVER, except that the Owner Trustee hereby represents, warrants and covenants to the Equity Participant that it will comply with the last sentence of Section 5.04, and (ii) no representation or warranty as to the validity or enforceability of any Transaction Document or as to the correctness of any statement made by any Person other than the Owner Trustee, contained in any thereof, and except that the Owner Trustee represents, warrants and covenants to the Equity Participant that this Agreement has been and each of such other documents which contemplates execution thereof by the Owner Trustee has been or will be executed and delivered by its

officers who are, or will be, duly authorized to execute and deliver such documents on its behalf.

SECTION 6.04. No Segregation of Moneys; No Interest.

Except as otherwise provided herein or in any of the Transaction Documents, moneys received by the Owner Trustee hereunder need not be segregated in any manner, except to the extent required by law, and may be deposited under such general conditions as may be prescribed by law, and the Owner Trustee shall not be liable for any interest thereon, except as may be agreed to by the Owner Trustee.

SECTION 6.05. Reliance; Advice of Counsel. The Owner Trustee shall not incur any liability to any Person in acting upon any signature, instrument, notice, resolution, request, consent, order, certificate, report, opinion, bond or other document or paper believed by it to be genuine and believed by it in good faith to be signed by the proper party or parties. The Owner Trustee may accept a certified copy of a resolution of the board of directors or other governing body of any corporate party as conclusive evidence that such resolution has been duly adopted by such body and that the same is in full force and effect. As to any fact or matter the manner of ascertainment of which is not specifically prescribed herein, the Owner Trustee may for all purposes hereof rely on an Officers' Certificate of the relevant party as to such fact or matter, and such certificate shall constitute full protection to the Owner Trustee for any action taken or omitted to be taken by it in good faith in reliance thereon. In the administration of the trusts hereunder, the Owner Trustee may execute any of the trusts or powers hereof and perform its powers and duties hereunder directly or through agents or attorneys and may consult with counsel, accountants and other skilled Persons to be selected and employed by it, and the Owner Trustee shall not be liable for anything done, suffered or omitted in good faith by it in accordance with the advice or opinion within the scope of such Person's competence of any such counsel, accountants or other skilled Persons and not contrary to this Agreement.

SECTION 6.06. Not Acting in Individual Capacity. Except as provided in this Article VI, in accepting the trusts hereby created the Owner Trustee acts solely as trustee hereunder and not in its individual capacity; and all Persons having any claim against the Owner Trustee by reason of the transactions contemplated by the Transaction Documents shall look only to the Trust Estate (or a part thereof, as the case may be) for payment or satisfaction thereof, except as specifically provided in this Article VI and except to the extent the Owner Trustee shall otherwise agree in any Transaction Document to which it is a party.

ARTICLE VII

INDEMNIFICATION OF THE OWNER TRUSTEE BY THE EQUITY PARTICIPANT

SECTION 7.01. The Equity Participant To Indemnify the Owner Trustee. The Equity Participant agrees to assume liability for, and to indemnify and hold harmless the Owner Trustee and FNB, in its individual capacity, against and from, any and all Claims which may be imposed on, incurred by or asserted at any time against the Owner Trustee (and not indemnified by the Lessee within a reasonable time after demand therefor) in any way relating to or arising out of the Trust Estate, any of the properties included therein, the administration of the Trust Estate or any action or inaction of the Owner Trustee hereunder or under the Transaction Documents, except only that the Equity Participant shall not be required to indemnify the Owner Trustee for Claims arising or resulting from any of the matters described in the last sentences of Sections 5.04 and 6.01. The indemnities contained in this Section 7.01 shall survive the termination of this Agreement.

SECTION 7.02. Compensation and Expenses. The Owner Trustee shall receive as compensation for its services hereunder such ordinary fees as are fair, reasonable and customary for the performance of such services and as may heretofore and from time to time hereafter be agreed upon between the Equity Participant and the Owner Trustee. The Owner Trustee shall be entitled to be reimbursed for its reasonable expenses hereunder and to be compensated reasonably for any extraordinary services rendered hereunder.

ARTICLE VIII

TERMINATION OF TRUST AGREEMENT

SECTION 8.01. Termination of Trust Agreement. This Agreement and the trusts created hereby shall terminate and the Trust Estate shall, subject to the Participation Agreement, the Indenture and Article IV of this Agreement, be distributed to the Equity Participant, and this Agreement shall be of no further force or effect, upon the earlier of (i) the sale or other final disposition by the Owner Trustee of all property constituting part of the Trust Estate and the final distribution by the Owner Trustee of all moneys or other property or proceeds constituting part of the Trust Estate in accordance with the terms of Article IV and (ii) 21 years less one day after the death of the last survivor of all of the descendants living on the date of this Agreement of Joseph P. Kennedy, father of President John F. Kennedy, but if any such rights, privileges or options shall be or become valid under Applicable Law for a period subsequent to the 21st anniversary of the death of such last survivor

(or, without limiting the generality of the foregoing, if legislation shall become effective providing for the validity or permitting the effective grant of such rights, privileges and options for a period in gross exceeding the period for which such rights, privileges and options are hereinabove stated to extend and be valid), then such rights, privileges or options shall not terminate as aforesaid but shall extend to and continue in effect, but only if such nontermination and extension shall then be valid under Applicable Law, until such time as the same shall, under Applicable Law, cease to be valid.

SECTION 8.02. Termination at Option of the Equity Participant. Notwithstanding Section 8.01, this Agreement and the trusts created hereby shall terminate and the Trust Estate shall be distributed to the Equity Participant, and this Agreement shall be of no further force and effect, upon the election of the Equity Participant by notice to the Owner Trustee, if such notice shall be accompanied by the written agreement of the Equity Participant assuming all the obligations of the Owner Trustee under or contemplated by the Transaction Documents and all other obligations of the Owner Trustee incurred by it as trustee hereunder; provided, however, that no such election shall be effective until (i) the lien of the Indenture on the Lease Indenture Estate has been released, (ii) full payment of the principal of and premium, if any, and interest on the Notes has been made and (iii) any lien on the Trust Estate created pursuant to Section 7(b)(4) of the Participation Agreement has terminated. Such written agreement shall be reasonably satisfactory in form and substance to the Owner Trustee and shall release the Owner Trustee from all further obligations of the Owner Trustee hereunder and under the agreements and other instruments mentioned in the preceding sentence.

ARTICLE IX

SUCCESSOR OWNER TRUSTEES, CO-OWNER TRUSTEES AND SEPARATE OWNER TRUSTEES

SECTION 9.01. Resignation of the Owner Trustee; Appointment of Successor. (a) The Owner Trustee may resign at any time without cause by giving at least 30 days' prior written notice to the Equity Participant, the Indenture Trustee and the Lessee, such resignation to be effective on the acceptance of appointment by a successor Owner Trustee under Section 9.01(b). In addition, the Equity Participant may at any time remove the Owner Trustee with or without cause by an instrument in writing delivered to the Owner Trustee, such removal to be effective upon the acceptance of appointment by a successor owner trustee under Section 9.01(b). In case of the resignation or removal of the Owner Trustee, the Equity Participant may appoint a successor Owner Trustee by an instrument signed by the Equity Participant. If

a successor Owner Trustee shall not have been appointed within 30 days after the giving of written notice of such resignation or the delivery of the written instrument with respect to such removal, the Owner Trustee or the Equity Participant may apply to any court of competent jurisdiction to appoint a successor Owner Trustee to act until such time, if any, as a successor shall have been appointed and shall have accepted its appointment as above provided. Any successor Owner Trustee so appointed by such court shall immediately and without further act be superseded by any successor Owner Trustee appointed as above provided within one year from the date of the appointment by such court.

(b) Any successor Owner Trustee, however appointed, shall execute and deliver to the predecessor Owner Trustee an instrument accepting such appointment, and thereupon such successor Owner Trustee, without further act, shall become vested with all the estates, properties, rights, powers, duties and trusts of the predecessor Owner Trustee in the trusts hereunder with like effect as if originally named an Owner Trustee herein; but nevertheless, upon the written request of such successor Owner Trustee, such predecessor Owner Trustee shall execute and deliver an instrument transferring to such successor Owner Trustee, upon the trusts herein expressed, all the estates, properties, rights, powers, duties and trusts of such predecessor Owner Trustee, and such predecessor Owner Trustee shall duly assign, transfer, deliver and pay over to such successor Owner Trustee all moneys or other property then held by such predecessor Owner Trustee upon the trusts herein expressed.

(c) Any successor Owner Trustee, however appointed, shall be a bank or trust company incorporated and doing business within the United States of America and having a combined capital and surplus of at least \$50,000,000, if there be such an institution willing, able and legally qualified to perform the duties of Owner Trustee hereunder upon reasonable or customary terms.

(d) Any corporation into which the Owner 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 Owner Trustee shall be a party, or any corporation to which substantially all the corporate trust business of the Owner Trustee may be transferred, shall, subject to the terms of Section 9.01(c), be the Owner Trustee under this Agreement without further act.

SECTION 9.02. Co-Trustees and Separate Trustees.

Whenever the Owner Trustee or the Equity Participant shall deem it necessary or prudent in order either to conform to any law of any jurisdiction in which all or any part of the Trust Estate shall be situated or to make any claim or bring any suit with respect to the Trust Estate, the Notes or any Transaction Document, or the Owner Trustee or the Equity Participant shall be advised by counsel

satisfactory to it that it is so necessary or prudent, the Owner Trustee and the Equity Participant shall execute and deliver an agreement supplemental hereto and all other instruments and agreements, and shall take all other action, necessary or proper to constitute one or more Persons (and the Owner Trustee may appoint one or more of its officers) either as co-trustee or co-trustees jointly with the Owner Trustee of all or any part of the Trust Estate, or as separate trustee or separate trustees of all or any part of the Trust Estate, and to vest in such Persons, in such capacity, such title to the Trust Estate or any part thereof and such rights or duties as may be necessary or desirable, all for such period and under such terms and conditions as are satisfactory to the Owner Trustee and the Equity Participant. In case any co-trustee or separate trustee shall die, become incapable of acting, resign or be removed, the title to the Trust Estate and all rights and duties of such co-trustee or separate trustee shall, so far as permitted by law, vest in and be exercised by the Owner Trustee, without the appointment of a successor to such co-trustee or separate trustee.

ARTICLE X

SUPPLEMENTS AND AMENDMENTS

SECTION 10.01. Supplements and Amendments. At the written request of the Equity Participant, this Agreement shall be amended by a written instrument signed by the Owner Trustee and the Equity Participant, but if in the opinion of the Owner Trustee any instrument required to be so executed adversely affects any right, duty or liability of, or immunity or indemnity in favor of, it under this Agreement or any of the documents contemplated hereby to which it is a party, or would cause or result in any conflict with or breach of any terms, conditions or provisions of, or default under, its charter documents or by-laws or any document contemplated hereby to which it is a party, the Owner Trustee may in its sole discretion decline to execute such instrument, unless it shall have been provided an indemnity satisfactory to the Owner Trustee by the Equity Participant.

SECTION 10.02. Limitation on Amendments. Notwithstanding Section 10.01, the Owner Trustee shall not execute any amendment which might result in the trusts created hereunder being terminated (i) without the consent of the Indenture Trustee, prior to the release of the lien of the Indenture on the Lease Indenture Estate or prior to the payment in full of the principal of and premium, if any, and interest on the Notes or (ii) without the consent of the holder thereof, prior to the termination of any lien created pursuant to Section 7(b)(4) of the Participation Agreement.

ARTICLE XI

MISCELLANEOUS

SECTION 11.01. No Legal Title to Trust Estate in the Equity Participant. The Equity Participant shall not have legal title to any part of the Trust Estate. No transfer, by operation of law or otherwise, of any right, title or interest of the Equity Participant in and to the Trust Estate or hereunder shall operate to terminate this Agreement or the trusts hereunder or entitle any successor or transferee to an accounting or to the transfer to it of legal title to any part of the Trust Estate.

SECTION 11.02. Sale of Undivided Interest and/or Real Property Interest by the Owner Trustee is Binding. Any sale or other conveyance of the Undivided Interest, the Real Property Interest or any part thereof or any assignment of rights under the Assignment and Assumption by the Owner Trustee made pursuant to the terms of this Agreement or any other Transaction Document shall bind the Equity Participant and shall be effective to transfer and convey all right, title and interest of the Owner Trustee and the Equity Participant in and to the Undivided Interest, the Real Property Interest or any part thereof, or such rights under the Assignment and Assumption, as the case may be. No purchaser or other grantee shall be required to inquire as to the authorization, necessity, expediency or regularity of such sale or conveyance or as to the application of any sale or other proceeds with respect thereto by the Owner Trustee.

SECTION 11.03. Limitations on Rights of Others. Nothing in this Agreement, whether express or implied, shall be construed to give to any Person other than the Owner Trustee and the Equity Participant any legal or equitable right, remedy or claim under or in respect of this Agreement, any covenants, conditions or provisions contained herein or the Trust Estate, all of which are and shall be construed to be for the sole and exclusive benefit of the Owner Trustee and the Equity Participant.

SECTION 11.04. Notices. Unless otherwise expressly specified or permitted by the terms hereof, all notices hereunder shall be given as provided in the Participation Agreement.

SECTION 11.05. Severability. Any provision of this Agreement which is prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and any such prohibition or unenforceability in any jurisdiction shall not invalidate or render unenforceable such provision in any other jurisdiction.

SECTION 11.06. Limitation on the Equity Participant's Liability. The Equity Participant shall not have any liability for the performance of this Agreement except as expressly set forth herein.

SECTION 11.07. Separate Counterparts. This Agreement may be executed by the parties hereto in separate counterparts, each of which when so executed and delivered shall be an original, but all such counterparts shall together constitute but one and the same instrument.

SECTION 11.08. Successors and Assigns. All covenants and agreements contained herein shall be binding upon, and inure to the benefit of, the Owner Trustee and its successors and assigns and the Equity Participant and its successors and assigns, all as herein provided. Any request, notice, direction, consent, waiver or other instrument or action by the Equity Participant shall bind the successors and assigns of the Equity Participant.

SECTION 11.09. Transfer of Interests. Subject to the provisions of Section 15 of the Participation Agreement, the Equity Participant may assign, convey or otherwise transfer all or any part of its right, title and interest in and to this Agreement and the Trust Estate. In case of any such assignment, conveyance or transfer of less than all of the interest of the Equity Participant, (i) the transferor and transferee or transferees shall be severally obligated with respect to the indemnification obligations imposed under Section 7.01 in accordance with the interest held by each of them and (ii) appropriate amendments shall be made to this Agreement to provide for the situation in which there is more than one Equity Participant as may be agreed to by the transferor and transferee or transferees and consented to by the Owner Trustee. No such assignment, conveyance or transfer shall violate any provision of Applicable Law or create a relationship which would be in violation thereof. The Owner Trustee shall not be on notice of or otherwise be bound by any such assignment, conveyance or transfer until it shall have received an executed counterpart of the instrument of such assignment, conveyance or transfer.

SECTION 11.10. Headings. The headings of the various Articles and Sections herein are for convenience of reference only and shall not define or limit any of the terms or provisions hereof.

SECTION 11.11. Governing Law. This Agreement shall in all respects be governed by, and construed in accordance with, the laws of the State of New York, including all matters of construction, validity and performance, except to the extent that, pursuant to the laws of the State of Arizona, the laws of such State are mandatorily applicable hereto.

SECTION 11.12. Administration of Trust. The principal place of administration of the Trust shall be in Boston, Massachusetts.

SECTION 11.13. Performance by the Equity Participant. Any obligation of the Owner Trustee hereunder or under any Transaction Document or other document contemplated herein may be performed by the Equity Participant and any such performance shall not be construed as a revocation of the trusts created hereby.

SECTION 11.14. Conflict with Transaction Documents. If this Agreement (or any instructions given by the Equity Participant pursuant hereto) shall require that any action be taken with respect to any matter and any other Transaction Document (or any instructions duly given in accordance with the terms thereof) shall require that a different action be taken with respect to such matter, and such actions shall be mutually exclusive, the provisions of such other Transaction Document, in respect thereof, shall control.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective officers thereunto duly authorized, as of the day and year first above written.

EMERSON FINANCE CO.

By: _____

[Signature]
President

THE FIRST NATIONAL BANK OF BOSTON,

By: _____

Assistant Vice President

SECTION 11.12. Administration of Trust. The principal place of administration of the Trust shall be in Boston, Massachusetts.

SECTION 11.13. Performance by the Equity Participant. Any obligation of the Owner Trustee hereunder or under any Transaction Document or other document contemplated herein may be performed by the Equity Participant and any such performance shall not be construed as a revocation of the trusts created hereby.

SECTION 11.14. Conflict with Transaction Documents. If this Agreement (or any instructions given by the Equity Participant pursuant hereto) shall require that any action be taken with respect to any matter and any other Transaction Document (or any instructions duly given in accordance with the terms thereof) shall require that a different action be taken with respect to such matter, and such actions shall be mutually exclusive, the provisions of such other Transaction Document, in respect thereof, shall control.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective officers thereunto duly authorized, as of the day and year first above written.

EMERSON FINANCE CO.

By: _____
President

THE FIRST NATIONAL BANK OF BOSTON,

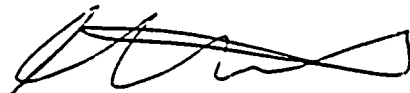
By: _____
Assistant Vice President

SECTION 15.6.1
LESSOR'S CERTIFICATE
APS Unit 2/1986-2

The undersigned, being a duly elected, qualified and acting Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association (FNB), hereby certifies, for and on behalf of FNB, as follows:

1. Reference is made to (i) the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, as amended (the ANPP Participation Agreement), and (ii) the sale and leaseback transaction proposed to be entered into by Arizona Public Service Company (APS) on or before August 20, 1986, with respect to Palo Verde Nuclear Generating Station (PVNGS) Unit 2 and APS's interest therein (the Proposed APS Sale and Leaseback Transaction);
2. In connection with the Proposed APS Sale and Leaseback Transaction, FNB will enter into a Trust Agreement (the Trust Agreement) with an affiliate of Emerson Electric Co. constituting FNB the trustee (in such capacity, Owner Trustee) of a grantor trust (the Grantor Trust); thereafter, the Grantor Trust will acquire from APS an undivided ownership interest of up to approximately 5.7% in certain assets constituting part of PVNGS Unit 2 and up to approximately 1.9% of the PVNGS site and lease back such interest to APS pursuant to a Facility Lease having a primary term of at least 25 years; and
3. Upon the execution and delivery of the Trust Agreement and upon consummation of the Proposed APS Sale and Leaseback Transaction, FNB, solely in its capacity as Owner Trustee and not otherwise, confirms that, except as provided in Sections 15.2.2, 15.6.4 and 15.10 of the ANPP Participation Agreement, APS shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Grantor Trust and any mortgagee, trustee and secured party of the Grantor Trust of the type described in Section 15.1.2 of the ANPP Participation Agreement) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of APS transferred to the Grantor Trust pursuant to the Proposed APS Sale and Leaseback Transaction.

WITNESS the signature of the undersigned this 8th day of August, 1986, for and on behalf of FNB.



Clark M. Whitcomb
Vice President

CERTAIN RIGHTS OF THE LESSOR UNDER THIS FACILITY LEASE HAVE BEEN ASSIGNED TO, AND ARE SUBJECT TO A SECURITY INTEREST IN FAVOR OF, CHEMICAL BANK, AS INDENTURE TRUSTEE UNDER A TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE, DATED AS OF AUGUST 1, 1986. THIS FACILITY LEASE HAS BEEN EXECUTED IN SEVERAL COUNTERPARTS. SEE SECTION 22(e) OF THIS FACILITY LEASE FOR INFORMATION CONCERNING THE RIGHTS OF HOLDERS OF VARIOUS COUNTERPARTS HEREOF.

THIS COUNTERPART IS NOT THE ORIGINAL COUNTERPART.

FACILITY LEASE

dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity,
but solely as Owner Trustee
under a Trust Agreement, dated as of August 1, 1986,
with Emerson Finance Co.

Lessor

and

ARIZONA PUBLIC SERVICE COMPANY

Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2
Emerson Finance Co.

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FACILITY LEASE

THIS FACILITY LEASE, dated as of August 1, 1986 between THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement, dated as of August 1, 1986, with Emerson Finance Co., as Lessor (the Lessor), and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, as Lessee (the Lessee).

W I T N E S S E T H :

WHEREAS, the Lessor owns the Undivided Interest and the Real Property Interest; and

WHEREAS, the Lessee desires to lease the Undivided Interest from the Lessor, and the Lessor is willing to lease the Undivided Interest and the Real Property Interest to the Lessee, all on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A hereto. References in this Facility Lease to sections, paragraphs and clauses are to sections, paragraphs and clauses in this Facility Lease unless otherwise indicated.

SECTION 2. Lease of Undivided Interest; Term; Personal Property.

(a) **Lease of Undivided Interest.** Upon the terms and subject to the conditions of this Facility Lease, the Lessor hereby leases to the Lessee, and the Lessee hereby leases from the Lessor, the Undivided Interest.

(b) **Term.** The term of this Facility Lease shall begin August 18, 1986, and shall end on the last day of the Lease Term.

(c) **Personal Property.** It is the express intention of the Lessor and the Lessee that title to the Undivided Interest and every portion thereof is severed, and shall be and remain severed, from title to the real estate constituting the Real Property Interest and the PVNGS Site. The Lessor and the Lessee intend that the Undivided Interest shall constitute personal property to the maximum extent permitted by Applicable Law.

(d) **Description.** The Undivided Interest is described on Schedule 6 hereto. The Real Property Interest is described on Schedule 7 hereto.

SECTION 3. Rent; Adjustments to Rent.

(a) **Basic Rent.** The Lessee shall pay to the Lessor, as basic rent (herein referred to as Basic Rent) for the Undivided Interest, the following amounts:

(i) on December 30, 1986, an amount equal to the daily equivalent of Basic Rent (set forth in Schedule 1 hereto) plus or minus any Rent Differential for the period from the Closing Date to and including December 31, 1986;

(ii) on June 30, 1987 and on each Basic Rent Payment Date thereafter to and including December 30, 2015, an amount equal to the percentage of Facility Cost set forth opposite such Basic Rent Payment Date in Schedule 1 hereto, plus or minus any Rent Differential;

(iii) if the Lessee shall elect the Fixed Rate Renewal Term, on June 30, 2016 and on each Basic Rent Payment Date thereafter during

the Fixed Rate Renewal Term, an amount equal to one-half of an amount determined by dividing an amount equal to the amount of all payments of Basic Rent payable with respect to the Basic Lease Term pursuant to clause (ii) of this Section 3(a) (taking into account the amount of any Rent Differential and any adjustments pursuant to Sections 3(d) and 3(e)), by 58; and

(iv) if the Lessee shall elect a Fair Market Renewal Term, on the first Basic Rent Payment Date in the Fair Market Renewal Term and on each Basic Rent Payment Date thereafter during the Fair Market Renewal Term, an amount equal to the greater of (A) the Fair Market Rental Value of the Undivided Interest and (B) the amount payable on each Basic Rent Payment Date during the Fixed Rate Renewal Term as determined pursuant to clause (iii) of this Section 3(a).

Payments made on December 30, 1986 and on each Basic Rent Payment Date shall be in satisfaction of the Lessee's obligation to pay Basic Rent for the six-month period ending on the last day of the month in which such Rent Payment Date shall have occurred (or the period commencing with the Closing Date and ending on December 31, 1986, in the case of the payment made on December 30, 1986). If an interest payment on any Note shall be due on a date other than December 30, 1986 or a Basic Rent Payment Date and the amount thereof is not included in a Refunding Loan being made on such date, the Lessee shall pay Basic Rent on such date equal to such interest payment and such payment of Basic Rent shall be credited against the Basic Rent due on December 30, 1986 or the Basic Rent Payment Date next succeeding the date that such additional Basic Rent shall have been paid.

(b) Supplemental Rent. The Lessee shall pay the following amounts (herein referred to as Supplemental Rent):

(i) when due or, where no due date is specified, on demand, any amount (other than Basic Rent, Casualty Value, Extraordinary Casualty Value and Special Casualty Value) which the Lessee assumes the obligation to pay

or agrees to pay to the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee or any Indemnatee under this Facility Lease, any other Transaction Document or any Collateral Trust Indenture and an amount equal to any amount which the Lessor is obligated to pay under Sections 6.9, 7.6 or 8.7 of the Indenture or under the Initial Series Notes other than principal and interest;

(ii) when due any amount payable hereunder as Casualty Value, Extraordinary Casualty Value or Special Casualty Value, and an amount equal to any premium or prepayment penalty with respect to the Notes;

(iii) on demand and in any event on the Basic Rent Payment Date next succeeding the date such amounts shall be due and payable hereunder, to the extent permitted by Applicable Law, interest (computed on the same basis as interest on the Notes is computed) at a rate per annum equal to (A) the Overdue Interest Rate, on that portion of the payment of Basic Rent or Supplemental Rent distributable pursuant to clause "first" of Section 5.1 or clause "second" of Section 5.3 of the Indenture (determined prior to the computation of interest on overdue payments referred to in such clauses), and (B) the Penalty Rate, on the balance of any such payment of Basic Rent or Supplemental Rent (including, without limitation, to the extent permitted by Applicable Law, interest payable pursuant to this clause (iii)) not paid when due (without regard to any period of grace) for any period for which the same shall be overdue.

The Lessor shall have all rights, powers and remedies provided for in this Facility Lease, at law, in equity or otherwise, in the case of non-payment of Basic Rent or Supplemental Rent. Drawings under the Letter of Credit shall be deemed to be in satisfaction of the Lessee's obligation to pay the Equity Portion of Rent hereunder to the extent of such drawing.

(c) Form of Payment. Subject to Section 11(b), each payment of Rent under this Facility Lease shall be made in immediately available funds no later than 12:00 noon, local time at the place of receipt, on the date each such payment shall be due and payable hereunder and shall be paid either (A) in the case of payments other than Excepted Payments, to the Lessor at its address determined in accordance with Section 17, or at such other address as the Lessor may direct by notice in writing to the Lessee, or (B) in the case of Excepted Payments, to such Person as shall be entitled to receive such payment at such address as such Person may direct by notice in writing to the Lessee. If the date on which any payment of Rent is due hereunder shall not be a Business Day, the payment otherwise due thereon shall be due and payable on the preceding Business Day, with the same force and effect as if paid on the nominal date provided in this Facility Lease.

(d) Adjustments to Rent for Change in Tax Law. Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values attached hereto shall be adjusted (upward or downward) to preserve Net Economic Return if there is any change in the Code or successor legislation adopted by the Ninety-ninth Congress and enacted into law (including technical corrections thereof and proposed, temporary or final regulations resulting therefrom) other than a change in respect of an "alternative minimum tax" (including any "add-on minimum tax having the same economic effect as an "alternative minimum tax"), and if H.R. 3838 is not adopted by the Ninety-ninth Congress, changes in Federal income tax rates are adopted by the One Hundredth Congress and enacted into law (herein referred to as a Change in Tax Law). Any adjustment under this Section 3(d) shall be made no more frequently than annually.

For purposes of determining whether a statutory or regulatory change constitutes a Change in Tax Law requiring adjustment pursuant to Section 3(d) and determining the effect thereof for purposes of making any adjustments required thereunder, the original Equity Participant shall be deemed to be the Equity Participant notwithstanding any transfer of its interest as such (whether or not permitted by Section 15 of the Participation Agreement); provided, however, that a successor Equity Participant shall be treated as the

Equity Participant for such purposes if the transfer to such successor Equity Participant was permitted by Section 15 of the Participation Agreement and if both the original Equity Participant and such successor Equity Participant are members of the same affiliated group of corporations that files a consolidated return for Federal income tax purposes.

(e) Adjustments to Rent for Changes in Pricing Assumptions. Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values attached hereto shall be adjusted (upward or downward) to preserve Net Economic Return if there is any change in the Pricing Assumptions. Any adjustments pursuant to Section 3(d) or this Section 3(e) hereof also (i) shall satisfy the provisions of Revenue Procedure 75-21, Revenue Procedure 75-28, and any other applicable statutes, regulations, revenue procedures, revenue rulings or technical information releases relating to the subject matter of such revenue procedures, shall be made in a manner designed to avoid application of Section 467(b)(2) of the Code and any regulations thereunder or any other similar provision of Federal income tax law and otherwise shall not cause any adverse effect under any Federal income tax laws in effect at the time of such adjustment, (ii) shall not cause any adverse effect under current accounting standards for leveraged leases as provided in Statement of Financial Accounting Standards No. 13 and (iii) shall, to the extent possible and not inconsistent with the foregoing, minimize the net present value cost of the Basic Rent to the Lessee to the extent that the foregoing criteria are met.

(f) Computation of Adjustments. As soon as practicable after the occurrence of an event requiring an adjustment to Basic Rent, and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values attached hereto, pursuant to Sections 3(d) or (e), the Equity Participant shall make the necessary computations and furnish to the Lessee, any Loan Participant, the Lessor, the Indenture Trustee and any Collateral Trust Trustee the revised amounts and percentages (together with a certificate of the chief financial or other appropriate officer of the Equity Participant to the effect that such revised amounts and percentages comply with the method for adjustment described in such Sections), which amounts and percentages shall be

implemented upon the later of (i) delivery of such amounts and percentages and (ii) if the Letter of Credit is in effect, 30 days after the delivery thereof, and, in either case, effective as of the later of (y) the date of occurrence of the event requiring such adjustment or (z) if the Letter of Credit is in effect, the date on which notice of such adjustment is given to the bank which has issued the Letter of Credit (taking into account any payment of Basic Rent already made) and shall remain effective until changed in consequence of any verification procedure set forth below. Such revised amounts and percentages shall be subject to verification (at the Lessee's request) by the Equity Participant's nationally recognized independent public accountants, in which case such accountants shall either (i) confirm to the Lessee in writing that such revised amounts were computed on a basis consistent with the original calculations, or (ii) compute and provide to the Lessee, the Lessor, the Equity Participant, each Loan Participant, the Indenture Trustee and any Collateral Trust Trustee revised amounts and percentages which are on such a basis. The revised amounts and percentages, as so confirmed or computed if applicable, shall be conclusive and binding upon the Lessee, the Lessor, the Equity Participant, each Loan Participant and the Indenture Trustee. The cost of any such verification shall be borne by the Lessee, unless such accountants shall require a downward adjustment to the revised amounts and percentages originally provided by the Equity Participant which is greater than 10% of the amount of the adjustment to Basic Rent so provided, in which case such cost shall be paid by the Equity Participant. Each adjustment pursuant to Section 3(d) or 3(e) may, but need not, be evidenced by the execution and delivery of a supplement to this Facility Lease in form and substance satisfactory to the Lessee and the Equity Participant, but shall be effective as provided herein without regard to the date on which such supplement to this Facility Lease is so executed and delivered.

(g) Sufficiency of Basic Rent and Supplemental Rent. Notwithstanding any other provision of this Facility Lease or any other Transaction Document, (i) the amount of Basic Rent payable on December 30, 1986 and on each Basic Rent Payment Date during the Basic Lease Term shall be at least equal to the aggregate amount of principal, premium, if any, and accrued interest then payable (or payable on or before the last

day of the month in which such Basic Rent Payment Date shall have occurred) on all Notes then Outstanding and (ii) each payment of Casualty Value, Extraordinary Casualty Value and Special Casualty Value shall in no event be less (when added to all other amounts required to be paid by the Lessee under this Facility Lease in respect of any Event of Loss or Deemed Loss Event or termination of this Facility Lease) than an amount sufficient, as of the date of payment, to pay in full the principal of, and premium, if any, and interest on all Notes Outstanding on and as of such date of payment (taking into account any assumption of the Notes by the Lessee on the date such payment is due).

(h) Rent Differential. So long as any series of Notes shall be Outstanding which bears interest at a floating rate, each installment of Basic Rent payable on December 30, 1986 or a Basic Rent Payment Date shall be increased or decreased, as the case may be, by the Rent Differential. For purposes hereof, "Rent Differential" shall mean, as of December 30, 1986 or any Basic Rent Payment Date, the difference between (i) the aggregate amount of interest due and payable on the Notes on December 30, 1986 and on each Basic Rent Payment Date and (ii) the aggregate amount of interest indicated on Schedule 8 hereto for such date. If, as of December 30, 1986 or any Basic Rent Payment Date, (A) the amount determined in accordance with clause (i) of the immediately preceding sentence shall exceed the amount determined in accordance with clause (ii) of such sentence, the amount of Basic Rent due on such date shall be increased by the Rent Differential, and (B) the amount determined in accordance with such clause (ii) shall exceed the amount determined in accordance with such clause (i), the amount of Basic Rent due on such date shall be decreased by the Rent Differential.

(i) Lessee as Agent. Unless and until an Event of Default has occurred and been continuing hereunder, the Lessor hereby appoints the Lessee as its agent with respect to all matters relating to the election of interest rates and options with respect thereto under the Initial Series Notes.

SECTION 4. Net Lease.

This Facility Lease (as originally executed and as modified, supplemented and amended from time to time) is a net lease and the Lessee hereby acknowledges and agrees that the Lessee's obligation to pay all Rent hereunder, and the rights of the Lessor in and to such Rent, shall be absolute, unconditional and irrevocable and shall not be affected by any circumstances of any character, including, without limitation, (i) any set-off, abatement, counterclaim, suspension, recoupment, reduction, defense or other right or claim which the Lessee may have against the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp, the Operating Agent, any ANPP Participant, any vendor or manufacturer of any equipment or assets included in the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site, PVNGS, or any part of any thereof, or any other Person for any reason whatsoever, (ii) any defect in or failure of the title, merchantability, condition, design, compliance with specifications, operation or fitness for use of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, (iii) any destruction of, damage to, or removal, abandonment, shutdown, salvage, scrapping, requisition, taking, loss, theft or destruction of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, or any interference, interruption or cessation in the use or possession thereof or of the Undivided Interest by the Lessee or by any other Person (including, without limitation, the Operating Agent or any other ANPP Participant) for any reason whatsoever or of whatever duration, (iv) any restriction, prevention or curtailment of or interference with any use of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, (v) any insolvency, bankruptcy, reorganization or similar proceeding by or against the Lessee, the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp, the Operating Agent, any other ANPP Participant or any other Person, (vi) the invalidity, illegality or unenforceability of this Facility Lease, any other Transaction Document, any Financing Document, the ANPP

Participation Agreement or any other instrument referred to herein or therein or any other infirmity herein or therein or any lack of right, power or authority of the Lessor, the Lessee, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp or any other Person to enter into this Facility Lease, any other Transaction Document or any Financing Document, or any doctrine of force majeure, impossibility, frustration, failure of consideration, or any similar legal or equitable doctrine that the Lessee's obligation to pay Rent is excused because the Lessee has not received or will not receive the benefit for which the Lessee bargained, it being the intent of the Lessee to assume all risks from all causes whatsoever that the Lessee does not receive such benefit, (vii) the breach or failure of any warranty or representation made in this Facility Lease or any other Transaction Document or any Financing Document by the Lessor, the Equity Participant, Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp or any other Person, (viii) any amendment or other change of, or any assignment of rights under, this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, or any waiver, action or inaction under or in respect of this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, or any exercise or non-exercise of any right or remedy under this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, including, without limitation, the exercise of any foreclosure or other remedy under the Indenture, any Collateral Trust Indenture or this Facility Lease, or the sale of Unit 2, any Capital Improvement, the Undivided Interest, the Real Property Interest, the PVNGS Site or PVNGS, or any part thereof or any interest therein, or (ix) any other circumstance or happening whatsoever whether or not similar to any of the foregoing. The Lessee acknowledges that, by conveying the leasehold estate created by this Facility Lease to the Lessee and by putting the Lessee in possession of the Undivided Interest and the Real Property Interest, the Lessor has performed all of the Lessor's obligations under and in respect of this Facility Lease, except the covenant contained in Section 6(a). The Lessee hereby waives, to the extent permitted by Applicable Law, any and all rights which it may now have or which at any time hereafter may be

conferred upon it, by statute or otherwise, to terminate, cancel, quit or surrender this Facility Lease or to effect or claim any diminution or reduction of Rent payable by the Lessee hereunder, including, without limitation, the provisions of Arizona Revised Statutes Section 33-343, except in accordance with the express terms hereof. If for any reason whatsoever this Facility Lease shall be terminated in whole or in part by operation of law or otherwise, except as specifically provided herein, the Lessee nonetheless agrees to pay to the Lessor or other Person entitled thereto an amount equal to each installment of Basic Rent and all Supplemental Rent at the time such payment would have become due and payable in accordance with the terms hereof had this Facility Lease not been terminated in whole or in part. Each payment of Rent made by the Lessee hereunder shall be final and the Lessee shall not seek or have any right to recover all or any part of such payment from the Lessor or any other Person for any reason whatsoever. All covenants, agreements and undertakings of the Lessee herein shall be performed at its cost, expense and risk unless expressly otherwise stated. Nothing in this Section 4 or elsewhere shall be construed as a guaranty by the Lessee of any residual value in the Undivided Interest or the Real Property Interest or as a guaranty of the Notes or any Bonds. Any provision of Section 7(b)(2) or 8(c) of the Participation Agreement to the contrary notwithstanding, if the Lessee shall fail to make any payment of Rent to any Person when and as due (taking into account applicable grace periods), such Person shall have the right at all times, to the exclusion of the ANPP Participants, to demand, collect, sue for, enforce obligations relating to and otherwise obtain all amounts due in respect of such Rent.

SECTION 5. Return of the Undivided Interest; Disposition Services.

(a) Return of the Undivided Interest. Unless the Lessee has acquired the Undivided Interest as provided herein, on the Lease Termination Date, the Lessee will surrender possession of the Undivided Interest to the Lessor (or to a Person specified by the Lessor to the Lessee in writing not less than 6 months prior to the Lease Termination Date) with full rights as a "Transferee" and the sole "Participant" with respect to the Undivided Interest within the meaning of Section 15.10 of the ANPP Participation Agreement, and will

furnish to the Lessor: (i) copies certified by a senior officer of the Lessee of all Governmental Actions necessary to effect such surrender (including, without limitation, appropriate amendments to the License permitting the Lessor (without being required to change its business or corporate structure) and for such Person to possess the Undivided Interest without the continued involvement of the Lessee), which Governmental Action shall be in full force and effect and not subject to any judicial or administrative contest, challenge or review; (ii) if not previously executed and delivered by the Lessee, and if desired by the Lessor, a ground lease covering that portion of the PVNGS Site which is included in the Real Property Interest, which ground lease shall have a term ending on the date of reversion of the Real Property Interest and shall be otherwise reasonably satisfactory to the Lessor in replacement for the Real Property Interest; and (iii) an opinion of counsel (which may be Mudge Rose Guthrie Alexander & Ferdon, Snell & Wilmer or other counsel experienced in matters pertaining to the Governmental Actions required, reasonably satisfactory to the Equity Participant) to the effect that (A) the Lessee has obtained all Governmental Actions and actions under the ANPP Participation Agreement necessary to effect such surrender by the Lessee and receipt of possession by the Lessor (or to the Person so specified by the Lessor) of the Undivided Interest and the Real Property Interest, (B) the Lessor (or the Person specified by the Lessor) is a NRC Licensee and an ANPP Participant (with all rights and obligations attendant thereto) and no additional Governmental Action will be required in connection with the possession by the Lessor (or the Person specified by the Lessor) of the Undivided Interest and the Real Property Interest, (C) such Governmental Action is in full force and effect and not subject to any judicial or administrative contest, challenge or review and (D) to the extent the aforementioned ground lease is required, such ground lease (1) has been duly authorized, executed and delivered, (2) constitutes the legal, valid and binding obligation of the Lessee, (3) does not require the consent of any Person or such consent has been previously received and (4) is not inconsistent with any ANPP Project Agreement. At the time of such return the Lessee shall pay or have paid all amounts due and payable, or to become due and payable, by it as an ANPP Participant under each and every ANPP Project Agreement allocable or chargeable (whether or not payable during or after the Lease Term) to the

Undivided Interest in respect of any period or periods ending on or prior to the Lease Termination Date (including, without limitation, all amounts payable with respect to any and all Capital Improvements to Unit 2 or the PVNGS Site approved or authorized (without the concurrence of the Equity Participant) prior to the end of the Lease Term, whether or not implementation thereof has been completed on or prior to the Lease Termination Date), and the Undivided Interest shall be free and clear of all Liens (other than Permitted Liens described in clauses (i), (v) (other than those for which satisfactory arrangements for the payment thereof have been made and those arising by, through or under the Lessee alone), (vi), (vii) (other than those arising by, through, or under the Lessee alone), (ix) or (x) of the definition of such term) and in the condition and state of repair required by Section 8. In the event that on or prior to the Lease Termination Date there shall have occurred a default by any ANPP Participant (other than the Lessee) under the ANPP Participation Agreement and such default shall not have been cured by the defaulting ANPP Participant, then (x) the Lessee agrees to indemnify and hold the Lessor (and each successor, assign and transferee thereof) harmless against any and all obligations under the ANPP Participation Agreement with respect to contributions or payments required to be made thereby as a result of such default and (y) the Lessor (and each successor, assign and transferee thereof) agrees to reimburse the Lessee for all amounts paid by the Lessee pursuant to the foregoing clause (x) in respect of the period following the Lease Termination Date to the extent, but only to the extent, that the Lessor (or such successor, assign or transferee) shall have actually received net proceeds from the sale of the Generation Entitlement Share of the defaulting ANPP Participant as a result of the payment made by the Lessee pursuant to the foregoing clause (x), and, to the extent the Lessor (or such successor, assign or transferee) shall have received such proceeds, the amount to be reimbursed to the Lessee pursuant to this clause (ii) shall include interest at the Prime Rate from the date of any payment by the Lessee pursuant to the foregoing clause (i) through the date of reimbursement of such amount pursuant to this clause (ii).

(b) **Disposition Services.** The Lessee agrees that if it does not exercise its option to renew or purchase as provided in Sections 12 and 13, respectively, then during the last thirty-six months of

the Lease Term, the Lessee will fully cooperate with the Lessor in connection with the Lessor's efforts to lease or dispose of the Undivided Interest and the Real Property Interest, including using the Lessee's reasonable efforts to lease or dispose of the Undivided Interest and the Real Property Interest. The Lessor agrees to reimburse the Lessee for reasonable out-of-pocket costs and expenses of the Lessee incurred at the request of the Lessor or the Equity Participant in connection with such cooperation and such efforts, but only to the extent of proceeds actually received by the Lessor.

SECTION 6. Warranty of the Lessor.

(a) Quiet Enjoyment. The Lessor warrants that until the Lease Termination Date, if the Lessee is in compliance with each and every material term and provision of this Facility Lease and each other Transaction Document to be complied with by the Lessee, the Lessee's use and possession of Unit 2, including the Undivided Interest, shall not be interrupted by the Lessor or any Person claiming by, through or under the Lessor, and their respective successors and assigns.

(b) Disclaimer of Other Warranties. The warranty set forth in Section 6(a) is in lieu of all other warranties of the Lessor or the Equity Participant, whether written, oral or implied, with respect to this Facility Lease, Unit 2, any Capital Improvement, the Real Property Interest, PVNGS or the PVNGS Site. As among the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, the Indenture Trustee, any Collateral Trust Trustee, the Lessor and the Lessee, execution by the Lessee of this Facility Lease shall be conclusive proof of the compliance of Unit 2 (including any Capital Improvement), the Undivided Interest and the Real Property Interest with all requirements of this Facility Lease, and the Lessee acknowledges and agrees that (i) NEITHER THE LESSOR NOR THE EQUITY PARTICIPANT IS A MANUFACTURER OR A DEALER IN PROPERTY OF SUCH KIND AND (ii) THE LESSOR LEASES AND THE LESSEE TAKES THE UNDIVIDED INTEREST AND THE REAL PROPERTY INTEREST, AND SHALL TAKE EACH CAPITAL IMPROVEMENT, AND ANY PART THEREOF, AS IS AND WHERE IS WITH ALL FAULTS, and, until such time as the Indenture is discharged, subject to the lien of the Indenture Trustee, and neither the Lessor nor the Equity Participant shall be deemed to have made, and THE LESSOR

AND THE OWNER PARTICIPANT EACH HEREBY DISCLAIMS AND NEITHER THE LESSOR NOR THE EQUITY PARTICIPANT SHALL HAVE ANY DUTIES WITH RESPECT TO, ANY OTHER REPRESENTATION OR WARRANTY, EITHER EXPRESS OR IMPLIED, AS TO ANY MATTER WHATSOEVER, INCLUDING, WITHOUT LIMITATION, THE DESIGN OR CONDITION OF UNIT 2, ANY CAPITAL IMPROVEMENT, THE UNDIVIDED INTEREST, THE PVNGS SITE OR PVNGS, OR ANY PART THEREOF, THE MERCHANTABILITY THEREOF OR THE FITNESS THEREOF FOR ANY PARTICULAR PURPOSE, TITLE TO UNIT 2, ANY CAPITAL IMPROVEMENT, THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST, THE PVNGS SITE OR PVNGS, OR ANY PART THEREOF, THE QUALITY OF THE MATERIAL OR WORKMANSHIP THEREOF OR CONFORMITY THEREOF TO SPECIFICATIONS, FREEDOM FROM PATENT OR TRADEMARK INFRINGEMENT OR THE ABSENCE OF ANY LATENT OR OTHER DEFECTS, WHETHER OR NOT DISCOVERABLE, NOR SHALL THE LESSOR OR THE OWNER PARTICIPANT BE LIABLE FOR INCIDENTAL OR CONSEQUENTIAL DAMAGES (INCLUDING LIABILITY IN TORT, STRICT, ABSOLUTE OR OTHERWISE), it being agreed that all such risks, as among the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, any Collateral Trust Trustee, the Indenture Trustee, the Lessor and the Lessee, are to be borne by the Lessee. The provisions of this Section 6(b) have been negotiated, and, except to the extent otherwise expressly provided in Section 6(a), the foregoing provisions are intended to be a complete exclusion and negation of any representations or warranties by the Lessor, the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, any Collateral Trust Trustee or the Indenture Trustee, express or implied, with respect to Unit 2 (including any Capital Improvement), the Undivided Interest, the Real Property Interest, PVNGS or the PVNGS Site that may arise pursuant to any law now or hereafter in effect, or otherwise.

(c) Enforcement of Certain Warranties. The Lessor authorizes the Lessee (directly or through agents, including the Operating Agent), at the Lessee's expense, to assert for the Lessor's account, during the Lease Term, all of the Lessor's rights (if any) under any applicable warranty and any other claims (under this Facility Lease or any Purchase Document) that the Lessee or the Lessor may have against any vendor or manufacturer with respect to Unit 2 (including any Capital Improvement) or the Undivided Interest, and the Lessor agrees to cooperate, at the Lessee's expense, with the Lessee and the Operating Agent in asserting such rights. Any amount receivable (without regard to any

right of setoff or other similar right of any Person against the Lessee) by the Lessee as payment under any such warranty or other claim against any vendor or manufacturer (or, if such warranty or claim relates to the Undivided Interest or the Retained Assets, the portion of such received amount appropriately allocable to the Undivided Interest) shall be applied in accordance with Sections 9(g), (h) and (i).

SECTION 7. Liens.

The Lessee will not directly or indirectly create, incur, assume or permit to exist any Lien except Permitted Liens on or with respect to the Undivided Interest, the Real Property Interest, the Lessor's title thereto or any interest of the Lessor or Lessee therein (and the Lessee will promptly, at its own expense, take such action as may be necessary duly to discharge any such Lien, except Permitted Liens).

SECTION 8. Operation and Maintenance; Capital Improvements.

(a) Operation and Maintenance. The Lessee agrees that (A) Unit 2 will be maintained in such condition that Unit 2 will have the capacity and functional ability to perform, on a continuing basis (ordinary wear and tear excepted), in normal commercial operation, the functions and substantially at the ratings for which it was designed, (B) Unit 2 will be operated, serviced, maintained and repaired, and all necessary or useful parts and components thereof will be replaced, so that the condition and operating efficiency will be maintained and preserved, ordinary wear and tear excepted, in all material respects in accordance with (1) Prudent Utility Practice for items of similar size and nature, (2) such operating standards as shall be required to take advantage of and enforce all available warranties, (3) the terms and conditions of all insurance policies maintained in effect at any time with respect thereto and (4) the terms of the ANPP Participation Agreement, (C) Unit 2 will be used, possessed, operated and maintained in compliance with all material applicable Governmental Actions (including the License) affecting PVNGS or Unit 2 or the use, possession, operation and maintenance thereof and (C) the Lessee will otherwise act in accordance with the standards set forth in the ANPP Participation Agreement. The Lessee will comply with all its obligations under Applicable Law affecting

Unit 2, the Undivided Interest, PVNGS, the Real Property Interest and the PVNGS Site, and the use, operation and maintenance thereof. The Lessee agrees to (i) exercise its rights under the ANPP Participation Agreement so that there will always be an Operating Agent under the ANPP Participation Agreement and (ii) maintain in full force and effect a license from the NRC adequate for it to possess the Undivided Interest and the Real Property Interest, in each case under the circumstances contemplated by the ANPP Participation Agreement. The Lessee will keep and maintain proper books and records (i) relating to all Operating Funds (as defined in the ANPP Participation Agreement) provided by it to the Operating Agent under the ANPP Participation Agreement and (ii) relating to the application of such Operating Funds to the operation and maintenance of Unit 2 and the acquisition, construction and installation of Capital Improvements (upon receipt of the requisite information from the Operating Agent), all in accordance with the Uniform System of Accounts. The Lessor shall not be obliged in any way to maintain, alter, repair, rebuild or replace Unit 2, any Capital Improvement, the Undivided Interest or the Real Property Interest, or any part thereof, or, except as provided in Section 8(f), to pay the cost of alteration, rebuilding, replacement, repair or maintenance of Unit 2, any Capital Improvement, the Undivided Interest or the Real Property Interest, or any part thereof, and the Lessee expressly waives the right to perform any such action at the expense of the Lessor pursuant to any law at any time in effect.

(b) Inspection. The Lessor, the Equity Participant, the Indenture Trustee and any Collateral Trust Trustee shall have the right to inspect Unit 2 and the Retained Assets (subject, in each event, to the ANPP Participation Agreement, Applicable Law and applicable confidentiality undertakings and procedures established by the Operating Agent) at their expense. The Lessor and the Equity Participant shall have the right to inspect, at their expense, the books and records of the Lessee relating to PVNGS, and make copies of and extracts therefrom (subject as aforesaid) and may, at their expense, discuss the Lessee's affairs, finances and accounts with its executive officers, all at such times and as often as may be reasonably requested. None of the Lessor, the Equity Participant, the Indenture Trustee or any Collateral Trust Trustee shall have any duty whatsoever to make any inspection or inquiry

referred to in this Section 8(b) and shall not incur any liability or obligation by reason of not making any such inspection or inquiry.

(c) Capital Improvements. To the extent that Applicable Law or Prudent Utility Practice in respect of considerations of public health or safety requires that a Capital Improvement be made to Unit 2, the Lessee shall cause such Capital Improvement to be made in accordance with the ANPP Participation Agreement. If and to the extent required by the ANPP Participation Agreement, the Lessee shall, at its sole expense, promptly participate in the making of any Capital Improvement to Unit 2. Without the written consent of the Lessor, the Lessee shall not permit any Capital Improvement to be made during the last three years of the Lease Term unless the Lessee has exercised its option to purchase or renew as provided herein or unless (i) such Capital Improvement is reasonably expected to be completed prior to the end of the Lease Term, as determined by an independent engineer selected by the Lessee and reasonably acceptable to the Lessor, (ii) arrangements for the payment thereof satisfactory to the Equity Participant have been made and (iii) the Lessee is committed to pay the cost thereof (whether or not completed prior to the end of the Lease Term) in a manner satisfactory to the Equity Participant. The net proceeds of (i) any sale or other disposition of property removed from Unit 2 received (considering as part of such amount received any amount set off or deducted by any Person claiming a right against the Lessee to do so) by, or credited to the account of, the Lessee in accordance with the ANPP Participation Agreement and (ii) any insurance proceeds received (considering as part of such amount received any amount set off or deducted by any Person claiming a right against the Lessee to do so) for the account of the Lessor or the Lessee in respect of the loss or destruction of, or damage or casualty to, any such property, the Unit 2 Interest of such amount shall be applied as provided in Section 9(g), (h) or (i), as the case may be. The Unit 2 Interest in property at any time removed from Unit 2 shall remain the property of the Lessor, no matter where located, until such time as a Capital Improvement constituting a replacement of such property shall have been installed in Unit 2 or such removed property has been disposed of by the Operating Agent in accordance with the ANPP Participation Agreement. Simultaneously with such disposition by the Operating

Agent, title to the Unit 2 Interest in the removed property shall vest in the Person designated by the Operating Agent, free and clear of any and all claims or rights of the Lessor. Unless paragraph (3) of Section 8(e) shall be applicable, upon the incorporation of a Capital Improvement in Unit 2, without further act, (i) title to the Unit 2 Interest, in such Capital Improvement shall vest in the Lessor and (ii) such applicable undivided interest in such Capital Improvement shall become subject to this Facility Lease and be deemed to be part of the Undivided Interest for all purposes hereof to the same extent that the Lessor had a like undivided interest in the property originally incorporated or installed in Unit 2. The Lessee warrants and agrees that the Lessor's interest in all Capital Improvements shall be free and clear of all Liens, except Permitted Liens other than the type specified in clauses (ii), (iii) and (xii) of the definition thereof.

(d) Reports. To the extent permissible, the Lessee shall prepare and file in a timely fashion, or, where the Lessor shall be required to file, the Lessee shall prepare and deliver to the Lessor within a reasonable time prior to the date for filing, any reports with respect to Unit 2, the Undivided Interest or the condition or operation thereof that shall be required to be filed with any Governmental Authority. On or before March 1 of each year (commencing March 1, 1987) and on the Lease Termination Date, the Lessee shall furnish the Lessor and the Equity Participant with a report stating the total cost of all Capital Improvements and describing separately and in reasonable detail each Capital Improvement (or related group of Capital Improvements) made during the period from the date hereof to December 31, 1986, in the case of the first such report, and during the period from the end of the period covered by the last previous report to the December 31 prior to such report, in the case of subsequent reports. On or before March 1 in each year (commencing March 1, 1987) and at such other times as the Lessor or the Equity Participant shall reasonably request in writing, the Lessee will report in writing to the Lessor with respect to (i) the most recent annual capital expenditure budget submitted by the Operating Agent to the Lessee in accordance with the ANPP Participation Agreement and (ii) the current plans (if any) which the Lessee may have for the financing of the same under Section 8(f).

(e) Title to Capital Improvements. Title to the Unit 2 Interest in each Capital Improvement to Unit 2 shall vest as follows:

(1) in the case of each Nonseverable Capital Improvement, whether or not the Lessor shall have financed or provided financing (in whole or in part) for such Unit 2 Interest in such Capital Improvement by an Additional Equity Investment or a Supplemental Financing, or both, effective on the date such Capital Improvement shall have been incorporated or installed in Unit 2, the Lessor shall, without further act, acquire title to such Unit 2 Interest in such Capital Improvement;

(2) in the case of each Severable Capital Improvement, if the Lessor shall have financed (by an Additional Equity Investment or a Supplemental Financing, or both) the Unit 2 Interest of the cost of such Capital Improvement, the Lessor shall, without further act, acquire title to such undivided interest in such Capital Improvement; and

(3) in the case of each Severable Capital Improvement, if the Lessor shall not have financed (by either an Additional Equity Investment or a Supplemental Financing, or both) the Unit 2 Interest of the cost of such Capital Improvement, the Lessee shall retain title to such an undivided interest in such Capital Improvement.

Immediately upon title to such Unit 2 Interest in any Capital Improvement vesting in the Lessor pursuant to paragraph (1) or paragraph (2) of this Section 8(e), such Unit 2 Interest in such Capital Improvement shall, without further act, become subject to this Facility Lease and be deemed part of the Undivided Interest and Unit 2 for all purposes hereof.

(f) Funding of the Cost of Capital Improvements. Before placing in service any Capital Improvement to Unit 2 the cost of which exceeds \$100,000,000 in respect of the interests of all ANPP Participants, the Lessee shall give the Lessor and the Equity Participant reasonable advance notice thereof. The Equity Participant shall have the option, in its

sole discretion, of financing through the Lessor the Unit 2 Interest of the cost of any such Capital Improvement, or any other Capital Improvement presented to the Equity Participant for financing, including or not including the making of an investment by the Equity Participant (an Additional Equity Investment) and the issuance of Additional Notes, all on terms acceptable to the Lessee and the Equity Participant. If the Equity Participant does not finance, or arrange the financing of, the Unit 2 Interest of the cost of such Capital Improvement, the Lessee may cause the Lessor to issue, if and to the extent permitted by the Indenture, to one or more Persons (other than the Lessee or any Person affiliated with the Lessee within the meaning of section 318 of the Code) Additional Notes and to use the proceeds thereof to pay the applicable percentage of the cost of such Capital Improvement, subject, however, to the satisfaction of the following conditions:

(i) there shall be no more than one Supplemental Financing in any calendar year;

(ii) the sum of the Supplemental Financing Amounts in any calendar year shall equal or exceed the Unit 2 Interest of \$5,000,000;

(iii) the Lessee may include in any request for a Supplemental Financing only Capital Improvements not previously financed in any Supplemental Financing and which have been installed or affixed no earlier than three calendar years before the beginning of the calendar year in which such Supplemental Financing occurs;

(iv) the total amount of all Supplemental Financings during the Basic Lease Term shall not exceed the Lessor's Portion of \$200,000,000;

(v) unless waived by the Equity Participant, the Lessee shall, at the time of such Supplemental Financing, have outstanding at least one issue of its debt securities (which may include the Bonds) rated at least "investment grade", as determined by Standard & Poor's and Moody's, if the Lessee has debt securities rated by such rating organizations, or as determined by one of such rating

organizations, if the Lessee has debt securities rated by only one such organization, or, if neither of such rating organizations shall rate debt securities of the Lessee at the time, by any nationally recognized rating organization in the United States of America;

(vi) the sum of the Supplemental Financing Amount and any Additional Equity Investment shall not exceed that portion of the cost of Capital Improvements which, when financed, will constitute an addition to the Equity Participant's basis under Section 1012 or 1016 of the Code;

(vii) in the opinion of independent tax counsel to the Equity Participant, such Supplemental Financing shall not result in any adverse tax effect upon the Equity Participant or affect the status of the Facility Lease as a "true lease" for Federal income tax purposes, and the Equity Participant and the Lessee shall have agreed upon the amount and manner of payment of any indemnity payable by the Lessee as a consequence of such Supplemental Financing;

(viii) the Additional Notes shall have a final maturity date no later than December 30, 2015;

(ix) the Lessee shall have made such representations and warranties and covenants regarding the tax characteristics of the Lessor's undivided interest in each Capital Improvement as shall be mutually acceptable to the Lessee and the Equity Participant;

(x) appropriate adjustments to Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values shall have been agreed to by the Equity Participant to support the amortization of the Additional Notes issued in respect of such Supplemental Financing and to preserve Net Economic Return (without regard to any tax

benefits associated with such Capital Improvement);

(xi) the Lessee shall have paid to the Lessor an amount that on an After-Tax Basis will be equal to all out-of-pocket costs and expenses reasonably incurred by the Lessor or the Equity Participant and not financed as a part of such Supplemental Financing or reflected in adjustments to Basic Rent;

(xii) no Default or Event of Default shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred;

(xiii) the Lessee shall have entered into such agreements and shall have provided such tax indemnities, opinions, certificates and other documents as the Equity Participant shall reasonably request;

(xiv) unless and until the Indenture has been discharged, Additional Notes shall be issued under, and in compliance with the terms of, the Indenture; and

(xv) in the opinion of the Equity Participant, such Supplemental Financing shall not result in any material adverse effect on the Equity Participant's financial accounting position.

SECTION 9. Event of Loss; Deemed Loss Event.

(a) Damage or Loss. In the event that Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) shall become applicable, or an Event of Loss, a Requisition of Use or a Requisition of Title shall occur, or Unit 2 or any substantial part thereof shall suffer destruction, damage, loss, condemnation, confiscation, theft or seizure for any reason whatsoever, such fact shall promptly, and in any case within five Business Days following any such event, be reported by the Lessee to the Lessor and the Equity Participant.

(b) Repair. The Lessee shall promptly make any and all payments required of the Lessee under the

provisions of the ANPP Participation Agreement relating to damage or destruction or the like to Unit 2 or any portion thereof; provided, however, that the Lessee shall in no event be obligated to make or join in any agreement under Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) concerning repairs to or reconstruction of Unit 2.

(c) Payment of Casualty Value. On the date next following the occurrence of an Event of Loss specified in a notice from the Lessor to the Lessee, the Lessee shall pay to the Lessor all Basic Rent due on, or accrued Basic Rent to, such date, plus an amount equal to the excess of (x) Casualty Value, determined as of the date such payment is due, if such date is a Basic Rent Payment Date, or the immediately preceding Basic Rent Payment Date, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from such Basic Rent Payment Date to such date of payment, over (y) the unpaid principal amount of the Notes Outstanding on such date and assumed by the Lessee on such date, after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of such Notes on such date. If the Lessee shall have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued the Bank Exchange Notes as provided in such Section), the Lessor shall, as long as no Default or Event of Default shall have occurred and be continuing (and at any time after the occurrence of an Event of Loss the Lessor may):

(i) if Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) shall be applicable and the Lessee shall have declined, but one or more of the other ANPP Participants shall have elected, to reconstruct or restore Unit 2, as permitted by the ANPP Participation Agreement, Transfer the Undivided Interest and the Real Property Interest to such electing ANPP Participants, as required by, and in the proportions set forth in, the ANPP Participation Agreement, in which case any amounts received by the Lessee in respect of the Lessor's Portion of the "salvage value" purchase price payable by such ANPP Participant to the Lessee in respect of Unit 2 (considering as part of

such amount received any amount set off or deducted by such Person as a result of a claim or right against the Lessee shall be applied (A) to reduce the Lessee's obligation to pay the amounts required to be paid by the Lessee pursuant to this paragraph or, if already paid, to reimburse the Lessee for such payment, and (B) the balance if any, of such payments shall be divided between the Lessee and the Lessor as their interests may appear); or

(ii) in all other cases Transfer the Undivided Interest and the Real Property Interest to the Lessee.

If the Lessee shall have made such payment but shall not have assumed the obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued the Bank Exchange Notes as provided in such Section), the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount, payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding, and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law.

(d) Payment of Special Casualty Value. If events giving rise to a Deemed Loss Event shall occur, the party hereto having knowledge thereof shall promptly notify the other party of the occurrence thereof. At any time thereafter, the Lessor may demand, by written notice to the Lessee, that the Lessee pay, and the Lessee shall pay, on the date specified in such notice, to the Lessor all Basic Rent due on, or accrued Basic Rent to, such date, plus an amount equal to the excess of (x) Special Casualty Value, determined as of the date such payment is due, if such date is a Basic Rent Payment Date, or the immediately preceding Basic Rent Payment Date, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from such Basic Rent Payment Date to such date of payment, over (y) the unpaid principal amount of the Notes Outstanding on such date, after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of the Notes on such date. If the Lessee shall

have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or shall have issued Bank Exchange Notes as provided therein), the Lessor shall, so long as no Default or Event of Default shall have occurred and be continuing (and at any time after the occurrence of a Deemed Loss Event the Lessor may), Transfer the Undivided Interest and the Real Property Interest to the Lessee. If the Lessee shall have made such payment but shall not have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued Bank Exchange Notes as provided therein), the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount, payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes Outstanding, and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law.

(e) Requisition of Use. In the case of a Requisition of Use not constituting an Event of Loss, this Facility Lease shall continue, and each and every obligation of the Lessee hereunder and under each Transaction Document shall remain, in full force and effect. So long as no Default or Event of Default shall have occurred and be continuing, the Lessee shall be entitled to all sums received by reason of any such Requisition of Use for the period ending on the Lease Termination Date, and the Lessor shall be entitled to all sums received by reason of any such Requisition of Use for the period after the Lease Termination Date.

(f) Termination of Lease Term. Upon (but only upon) a Transfer by the Lessor pursuant to Section 9(c) or 9(d) to the Lessee, the Lessee's assumption of all remaining obligations and liabilities of the Owner Trustee under the Indenture and the Notes and payment of the amounts specified therein, the Lease Term shall end and the Lessee's obligation to pay Basic Rent after such Transfer shall cease, but the Lessee shall continue to be required to make all payments of Supplemental Rent as and when due. In all other cases, the Lease Term shall continue and this Facility Lease shall remain in full force and effect.

(g) Application of Payments on an Event of Loss. Any payments received at any time by the Lessor or the Lessee (other than insurance placed by the Owner Trustee or the Equity Participant pursuant to Section 10(b)) from any Governmental Authority, insurer or other Person (except the Lessee) as a result of the occurrence of an Event of Loss (considering as part of such amount received any amount which was set off or deducted therefrom as a result of a claim by any Person against the Lessee) shall be applied as follows:

(i) all such payments shall be promptly paid to the Lessor for application pursuant to the following provisions of this Section 9(g), except that the Lessee may retain any amounts that would at the time be payable to the Lessee as reimbursement under the provisions of clause (ii) below;

(ii) so much of such payments as shall not exceed the amount required to be paid by the Lessee pursuant to Section 9(c) (ignoring, for this purpose, clause (ii) of the first sentence thereof) shall be applied in reduction of the Lessee's obligation to pay such amount if not already paid by the Lessee or, if already paid by the Lessee, shall be applied to reimburse the Lessee for its payment of such amount; and

(iii) the balance, if any, of such payments, in the case of payments from insurance carried by or on behalf of the Lessee shall be paid to the Lessee or, in the case of any other payments, shall be divided between the Lessor and the Lessee as their interests may appear.

(h) Application of Payments Not Relating to an Event of Loss. Payments received (considering as part of such amount received any amount which was set off or deducted therefrom as a result of a claim by any Person against the Lessee) at any time by the Lessor, the Lessee or the Equity Participant (other than insurance placed by the Owner Trustee or the Equity Participant pursuant to Section 10(b)) from any insurer or other Person with respect to any event giving rise to an amount referred to in the second sentence of Section 6(c) or the third sentence of Section 8(c), destruction, damage, loss, condemnation, confiscation,

theft or seizure of or requisition of title to Unit 2, the Undivided Interest or the Real Property Interest or any part thereof, in each case not constituting an Event of Loss shall be applied first to reimburse the Lessee for all amounts expended by it pursuant to Section 9(b) and second, the balance, if any, of such payments shall, in the case of payments from insurance carried by or on behalf of the Lessee, be paid to the Lessee or, in the case of other payments, be divided between the Lessor and the Lessee as their interests may appear.

(i) Dispositions at Time of Default or Event of Default. Notwithstanding the foregoing provisions of this Section 9, if a Default or an Event of Default shall have occurred and be continuing, any amount that would otherwise be payable to or for the account of, or that would otherwise be retained by, the Lessee pursuant to Section 10 or this Section 9 shall be paid to the Lessor as security for the obligations of the Lessee under this Facility Lease and, at such time thereafter as the Lessee shall have cured any such Default or Event of Default, such amount shall be paid promptly to the Lessee unless this Facility Lease shall have theretofore been declared to be in default, in which event such amount shall be disposed of in accordance with the provisions hereof and of the Indenture.

SECTION 10. Insurance.

(a) Required Insurance. The Lessee will cause the Operating Agent to carry and maintain at least the following insurance coverage with respect to the Undivided Interest and the Real Property Interest, in each case with insurers of recognized responsibility, in such form as shall be satisfactory to the Equity Participant.

(1) Non-Nuclear Insurance. The Lessee shall maintain:

(i) "all risk" property insurance covering physical loss with respect to Unit 2 in such amounts and with such other terms as are required by or are in accordance with Prudent Utility Practice, but in no event shall such amounts be less than the estimated maximum probable loss in respect of such property. Any insurance carried in accordance with this

Section 10(a)(1)(i) shall be endorsed to provide that:

(A) losses shall be adjusted and paid as provided in Section 10(a)(4);

(B) the Lessor and the Equity Participant (the "Additional Insureds") (i) are included as additional insureds, as their interests may appear and (ii) any obligation imposed upon the insured (including without limitation the liability to pay premiums) shall be the sole obligation of the Lessee and not that of any Additional Insured;

(C) the respective interests of the Additional Insureds shall not be invalidated by any breach of any warranties by the ANPP Participants contained in such policies;

(D) the insurer thereunder waives all rights of subrogation against the Additional Insureds with respect to their respective interests in Unit 2;

(E) such insurance shall be primary without right of contribution of any other insurance carried by or on behalf of any Additional Insured with respect to its interest in Unit 2; and

(F) if such insurance is cancelled for any reason whatsoever including non-payment of premium or any substantial change is made in the coverage which affects the interest of the Additional Insureds, (1) such cancellation or change shall not be effective as to the Additional Insureds for 30 days after receipt by The First National Bank of Boston, as Owner Trustee and agent, of written notice from such insurer of such cancellation or change, and (2) the Lessee will use its best efforts to cause such insurer to deliver a certificate with respect to such cancellation or

change to the Equity Participant and the Indenture Trustee.

(ii) bodily injury and property damage liability insurance (including product liability, completed operations and personal injury insurance) covering claims arising out of the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site. The amount and other terms of such insurance shall be in accordance with the higher of Prudent Utility Practice and the ANPP Participation Agreement, but such limits shall in no event be less than \$25,000,000 per occurrence combined bodily injury and property damage. Such insurance may include deductible amounts not to exceed \$5,000,000. Any insurance carried in accordance with this Section 10(a)(1)(ii) shall be endorsed as provided in paragraphs (B), (C), (D), (E) and (F) of Section 10(a)(1)(i), except that the term "Additional Insureds" wherever it appears shall include the Lessor, the Equity Participant and all Indemnitees.

(2) Nuclear Insurance. The Lessee shall maintain:

(i) nuclear property insurance in amounts and with such other terms as are required by or are in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement and (c) Prudent Utility Practice; provided, however, that such insurance shall at all times be maintained in amounts at least equal to the maximum nuclear property insurance available on commercially reasonable terms. The coverage afforded by such nuclear property insurance in respect of any loss at PVNGS and available for any loss at Unit 2, either (A) shall at all times be at least equal to \$750 million regardless of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of Nuclear Incident) or (B) so long as (1) Unit 2 is in, or is in a procedure which will result in, a state of cold shutdown in accordance with Prudent Utility Practice and (2) the first mortgage

bonds of the Lessee shall have an investment grade rating (x) by two nationally accepted rating agencies if such first mortgage bonds are rated by two nationally accepted rating agencies or (y) by one nationally accepted rating agency if such first mortgage bonds are only rated by one nationally accepted rating agency, will be reinstated to be equal to at least \$750 million within 180 days of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of a Nuclear Incident). Such insurance may include deductible amounts not to exceed \$10,000,000. Any insurance carried in accordance with this Section 10(a)(2)(i) shall be endorsed by the insurer as provided in paragraphs (A), (B), (D), (E) and (F) of Section 10(a)(1)(i).

(ii) the maximum nuclear liability insurance in amounts and such other terms as required by or in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement, (c) Prudent Utility Practice and (d) the maximum nuclear liability insurance available on commercially reasonable terms, but in any event in such amounts and containing such other terms as to cover the "aggregate liability" for a single "nuclear incident" of all "persons indemnified" (as such terms are used in the Atomic Energy Act) and in connection with the ownership, maintenance, condition or use of Unit 2 and the PVNGS Site. The Lessee shall also maintain supplier's and transporter's insurance in amounts consistent with Prudent Utility Practice. The Lessee shall maintain nuclear liability insurance pursuant to this Section 10(a)(2)(ii), whether or not the Lease Termination Date shall have occurred, until notified by the Equity Participant that neither the Lessor nor the Equity Participant has any further real or potential liability in connection with the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site; provided that after Decommissioning has been completed the Lessee shall not be required to maintain nuclear liability insurance for more than 30 years.

Any insurance carried in accordance with this Section 10(a)(2)(ii) shall be endorsed as provided in paragraphs (B), (D), (E) and (F) of Section 10(a)(1)(i).

(iii) the Lessee shall, or shall cause the Operating Agent to, use its best efforts at all times to obtain the endorsement referred to in paragraph (C) of Section 10(a)(1)(i) on all insurance referred to in this Section 10(a)(2), and shall cause such endorsement to be obtained if and to the extent it is available to any other owner or operator of a nuclear generating unit.

(3) Annual Reports and Certificates. The Lessee shall, on or before March 1 of each year, commencing March 1, 1987, furnish to the Lessor and the Equity Participant (A) a report signed by the broker or brokers for the PVNGS insurance (or if insurance is placed directly by the Operating Agent, a report signed by the Operating Agent which will include a copy of the certificate of insurance signed by the carrier, which certificate shall indicate that all endorsements required by this Section 10 are applicable) (i) describing in detail the insurance then maintained by the ANPP Participants with respect to PVNGS, (ii) stating that no premiums are then delinquent, and (iii) stating that insurance maintained is in accordance with (1) the ANPP Participation Agreement and (2) this Section 10; (B) a report signed by the broker or brokers for the Lessee's insurance (or if insurance is placed directly by the Lessee, a report signed by the Lessee which will include a copy of the certificate of insurance signed by the carrier, which certificate shall indicate that all endorsements required by this Section 10 are applicable) showing the separate insurance, if any, then maintained by the Lessee with respect to its interest in PVNGS and stating that no premiums under such insurance are delinquent; (C) a certificate signed by the Lessee stating that the insurance maintained by the ANPP Participants and by the Lessee, identified on the reports to be delivered pursuant to clauses (A) and (B), is in accordance with Prudent Utility Practice within the nuclear industry, the ANPP Participation Agreement and this Section 10; and (D) upon the request of the Lessor or the Equity

Participant, copies (to the extent permitted by the issuers of such policies) of policies so maintained. Any report by an insurance broker with respect to clause (A)(iii)(1) may be made in reliance upon a schedule provided by the Lessee (a copy of which shall be attached) identifying the insurance (by coverage, limits, insureds and other pertinent details) required to be maintained under the ANPP Participation Agreement. Any report with respect to clause (A)(iii)(2) may be made in reliance upon a similar schedule provided by the Lessee (a copy of which shall be attached) identifying the insurance required to be maintained under this Section 10.

(4) Proceeds. All insurance proceeds paid in respect of or pursuant to paragraphs (1) and (2) above shall (i) be applied as provided in Section 9(g), (h) or (i), as the case may be, and (ii) be adjusted with the insurance companies or otherwise collected, including the filing of appropriate proceedings, by the Operating Agent in accordance with the ANPP Participation Agreement, subject, however, to any priority allocations of such proceeds to decontamination and debris removal set forth in the insurance policies or required under Applicable Law. If the Operating Agent, as trustee, shall become the loss payee under any policy of insurance constituting "Project Insurance", as such term is defined in the ANPP Participation Agreement, then the Lessor and the Equity Participant shall be made beneficiaries of the trust arrangement under which the Operating Agent acts as trustee.

(b) Permitted Insurance. Nothing in this Section 10 shall prohibit the Lessee from placing at its expense insurance on or with respect to the cost of purchasing replacement power, naming the Lessee as insured and/or loss payee, unless such insurance would conflict with or otherwise limit the availability of insurance to be provided or maintained in accordance with Section 10(a). Nothing in this Section 10 shall prohibit the Lessor or the Equity Participant from placing at its expense other insurance on or with respect to Unit 2, the Undivided Interest or the Real Property Interest or the operation of Unit 2, naming the Lessor or the Equity Participant as insured and/or loss payee, unless such insurance would conflict with or otherwise limit the

insurance to be provided or maintained in accordance with Section 10(a).

SECTION 11. Rights to Assign or Sublease.

(a) Assignment or Sublease by the Lessee. Without the prior written consent of the Lessor, the Lessee shall not encumber (except for Permitted Liens), or assign, sublease or transfer (except to a Surviving Lessee in a transaction which meets the requirements of Section 10(b)(3)(ii) of the Participation Agreement), its leasehold interest under this Facility Lease in the Undivided Interest or the Real Property Interest, except that the Lessee may assign its leasehold interest under this Facility Lease in the Undivided Interest and the Real Property Interest to a wholly owned subsidiary of the Lessee or of the Lessee's parent if such subsidiary's obligations under this Facility Lease and the other Transaction Documents and the Financing Documents, if then in effect, shall be guaranteed by APS pursuant to a valid and enforceable guarantee containing appropriate covenants of APS and otherwise satisfactory in form and substance to the Equity Participant in its absolute discretion. The Lessee shall not, without the prior written consent of the Lessor and the Equity Participant, part with the possession of, or suffer or allow to pass out of its possession, the Undivided Interest or the Real Property Interest or any interest therein, except to the extent required pursuant to the ANPP Participation Agreement or as expressly permitted by the provisions of this Facility Lease (including, without limitation, the first sentence of this Section 11(a)).

(b) Assignment by Lessor as Security for Lessor's Obligations. To secure the indebtedness evidenced by the Notes, the Lessor will assign to the Indenture Trustee (x) its right, title and interest in and to this Facility Lease, including the right to receive all payments of Rent (other than Excepted Payments and Excepted Rights), to the extent provided in the Indenture and (y) its right, title and interest in and to the Undivided Interest and the Real Property Interest. The Lessee hereby (a) consents to such assignment and to the terms of the Indenture, (b) agrees to pay directly to the Indenture Trustee at the Indenture Trustee's Office (so long as the lien of the Indenture has not been satisfied and discharged and the Lessor is obligated thereunder) all amounts of Rent

(other than Excepted Payments) due or to become due to the Lessor that shall be required to be paid to the Indenture Trustee pursuant to the Indenture, (c) agrees that the right of the Indenture Trustee to any such payments shall be absolute and unconditional and shall not be affected by any circumstances whatsoever, including, without limitation, those circumstances set forth in Section 4, and (d) agrees that, to the extent provided in the Indenture and until the Indenture is discharged in accordance with its terms, the Indenture Trustee shall have all the rights of the Lessor hereunder (other than Excepted Rights and the right to receive Excepted Payments) as if the Indenture Trustee had originally been named herein as the Lessor. Following any Transfer by Lessor or purchase by Lessee of the Undivided Interest and the Real Property Interest, the Undivided Interest and the Real Property Interest shall (unless the Notes shall have been paid in full) remain subject to the lien of the Indenture and such lien shall continue as an existing, valid and enforceable first lien on the Undivided Interest and the Real Property Interest.

SECTION 12. Lease Renewal.

(a) Fixed Rate Renewal Term. Subject to the notice requirements set forth in Section 13(a), at the end of the Basic Lease Term, provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee shall have the right to renew the term of this Facility Lease (i) for a period commencing January 1, 2016, and ending midnight on December 31, 2017 (such period and any extension thereof pursuant to clause (ii) of this paragraph (a) being herein referred to as the Fixed Rate Renewal Term); and (ii) if it has elected the Fixed Rate Renewal Term, for an extension period commencing on January 1, 2018 and which expires not later than the last day of the Maximum Option Period.

(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of

Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period not to exceed 2 years (herein referred to as the Fair Market Renewal Term; and the Fixed Rate Renewal Term (including any extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in which case Basic Rent payable during such Fair Market Renewal Term shall be the Fair Market Rental Value of the Undivided Interest.

SECTION 13. Notices for Renewal or Purchase; Purchase Options.

(a) Expiration of Basic Lease Term. Not earlier than five nor later than three years prior to the expiration date of the Basic Lease Term the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(a) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration date of the Basic Lease Term as the case may be, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(b) or (y) the option to renew this Facility Lease for the Fixed Rate Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor if, on the date a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(a), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such Fair Market Sales Value shall be determined by the Appraisal Procedure. In the case of the exercise of the option for the Fixed Rate Renewal Term, the Maximum Option Period shall be determined by the Appraisal Procedure.

(b) Expiration of Fixed Rate Renewal Term. Not earlier than five years and later than three years prior

to the expiration date of the Fixed Rate Renewal Term, if elected, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(b) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration of the Fixed Rate Renewal Term the Lessee will give the Lessor written notice of its election to exercise (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fair Market Renewal Term. Any such election shall be irrevocable as to the Lessee (except as hereinafter provided), but no such election shall be binding on the Lessor, if, on the effective date thereof, an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(b), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value and the Fair Market Rental Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such values shall be determined by the Appraisal Procedure.

(c) Purchase Option at Expiration of the Lease Term. Subject to the notice requirements set forth in Section 13(a) or 13(b), as the case may be, provided that no Event of Default shall have occurred and be continuing, no Event of Loss or Deemed Loss Event shall have occurred and the Notes shall have been paid in full, the Lessee shall have the right to purchase the Undivided Interest on the date of the expiration of the Basic Lease Term or the then applicable Renewal Term (if elected), for a purchase price equal to the Fair Market Sales Value thereof.

(d) Purchase of the Undivided Interest; Payment, Etc. If the Lessee shall have elected to purchase the Undivided Interest pursuant to Section 13(c), payment by the Lessee of the purchase price therefor shall be made in immediately available funds, whereupon

the Lessor shall Transfer the Undivided Interest and the Real Property Interest to the Lessee.

(e) Acquisition of Additional Capacity. The Lessee agrees not to acquire or lease any additional capacity from PVNGS during the five years preceding the expiration of the Basic Lease Term unless at the time of such acquisition or lease, the Lessee has exercised its option to renew this Facility Lease or purchase the Undivided Interest.

SECTION 14. Termination for Obsolescence.

(a) Termination Notice. Unless a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred, if the Board of Directors of the Lessee shall have adopted a resolution to the effect that Unit 2 is surplus to the Lessee or economically obsolete and provided that the Lessee is making a good faith effort to sell any ownership interest which it may have in Unit 2, the Lessee shall deliver a written notice (a Termination Notice) to the Lessor, the Equity Participant and the Indenture Trustee (which notice shall be irrevocable), to terminate this Facility Lease on any Basic Rent Payment Date after December 30, 1996, and prior to December 30, 2012 (the Termination Date), which date shall not be earlier than one year from the date of such notice. If the Lessee shall give the Lessor a Termination Notice, the Lessee shall, as agent for the Lessor, use its best efforts to obtain cash bids for the purchase of the Undivided Interest and the Real Property Interest, together with the interest of the Lessor under the Assignment and Assumption. The Lessor shall also have the right to obtain such cash bids, either directly or through agents other than the Lessee. The Lessee shall certify to the Lessor within ten days after the Lessee's receipt of each bid (and, in any event, prior to the Termination Date) the amount and terms thereof and the name and address of the Person (which shall not be the Lessee or any Affiliate of the Lessee or any agent of any thereof) submitting such bid.

(b) Right of Lessor to Retain Undivided Interest upon Termination. The Lessor may elect to retain, rather than sell, the Undivided Interest and the Real Property Interest by giving notice to the Lessee and the Indenture Trustee prior to the Termination Date. It shall be a condition precedent to the Lessor's

right to retain the Undivided Interest and the Real Property Interest that on or prior to the Termination Date the Lessor shall have paid (or made provision for payment) to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on such date and all premium, if any, and interest accrued and unpaid on the date of payment. If the Lessor elects to retain the Undivided Interest and the Real Property Interest pursuant to this Section 14(b), the Lessee shall pay to the Lessor on the Termination Date the Basic Rent and any other Rent due or accrued, as the case may be, to and including the Termination Date, together with an amount equal to the excess, if any, of the Special Casualty Value as of the Termination Date over the highest bona fide offer received pursuant to Section 14(a).

(c) Events on the Termination Date. If the Lessor has not elected to retain the Undivided Interest as provided in Section 14(b), on the Termination Date the Lessor shall (but only upon receipt of the sale price and all additional payments specified in the next sentence) Transfer the Undivided Interest for cash to the bidder (which shall not be the Lessee or an Affiliate of the Lessee or any agent of any thereof) that shall have submitted the highest bid on or before the Termination Date. The total sale price realized at such sale shall be retained by the Lessor (subject, however, to the terms of the Indenture and the requirement that there shall have been paid, or provision for payment made, to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on the Termination Date and all premium, if any, and interest accrued and unpaid on the date of payment) and, in addition, on the Termination Date the Lessee shall pay to the Lessor (A) the excess, if any, of the Special Casualty Value as of the Termination Date over the net sale price of the Undivided Interest and (B) any Basic Rent due or accrued, as the case may be, to and including the Termination Date, and shall pay to the Person or Persons entitled thereto all Supplemental Rent (other than Special Casualty Value). Upon compliance by the Lessee with the applicable provisions of this Section 14, the obligation of the Lessee to pay Basic Rent for any period after the Termination Date shall cease and the Basic Lease Term shall end on the Termination Date but the obligations of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination. If, other than as a result of the Lessor's

election to retain the Undivided Interest and the Real Property Interest as provided in Section 14(b), on or as of the Termination Date no such sale shall occur or the Lessee shall not have complied in full with this Section 14, this Facility Lease shall continue in full force and effect in accordance with its terms except that the Lessee shall be entitled to deliver one other Termination Notice provided that such second Termination Notice shall not occur during the 3-year period following such Termination Date. The Lessor shall be under no duty to solicit bids, to inquire into the efforts of the Lessee to obtain bids or otherwise take any action in connection with any such sale, other than, if the Lessor has not elected to retain the Undivided Interest, to Transfer the Undivided Interest and the Real Property Interest to the purchaser named in the highest bid certified by the Lessee to the Lessor or obtained by the Lessor, against receipt of the payments provided for herein.

(d) Early Termination. If the Lessee shall fail to exercise its renewal option or purchase option within the time provided by Section 13(a) or 13(b), the Lessor shall have the option, on any Basic Rent Payment Date thereafter, on at least one year's prior written notice (an Early Termination Notice) to the Lessee and the Indenture Trustee, to terminate this Facility Lease on the Basic Rent Payment Date specified in such notice (the Early Termination Date). Any Early Termination Notice may be revoked by the Lessor at any time on or prior to the 30th day preceding the Early Termination Date (the Early Termination Commitment Date), after which the Lessor shall be irrevocably committed to terminate this Facility Lease on the Early Termination Date. On or prior to the Early Termination Commitment Date, the Lessor shall deposit with the Indenture Trustee cash in an amount (or a letter of credit of an Eligible Bank for such amount) equal to the unpaid principal amount of all Notes outstanding on such date and all premium, if any, and interest accrued and to accrue on and as of the Early Termination Date. On the Early Termination Date, the Lessee shall pay to the Lessor any Basic Rent due or accrued, as the case may be, to and including the Early Termination Date, and shall pay to the Person or Persons entitled thereto all Supplemental Rent (excluding from such Supplemental Rent any amount due and owing with respect to principal of, and premium, if any, on the Notes being prepaid on such date, other than any amount of principal which would have been paid

on such date if such Notes were not being prepaid), whereupon the obligation of the Lessee to pay any Basic Rent for any period after the Early Termination Date shall cease and the Lease Term shall end, but the obligations of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination.

SECTION 15. Events of Default.

The term Event of Default, wherever used herein, shall mean any of the following events (whatever the reason for such Event of Default and whether it shall be voluntary or involuntary, or come about or be effected by operation of law, or be pursuant to or in compliance with any Applicable Law or Governmental Action):

(i) the Lessee shall fail to make, or cause to be made, (x) payment of Casualty Value, Extraordinary Casualty Value or Special Casualty Value when due or payment due pursuant to exercise of the Cure Option when due, (y) any payment of Basic Rent within 5 days after the same shall become due or (z) any payment of Supplemental Rent (other than Casualty Value, Extraordinary Casualty Value or Special Casualty Value, or payment due pursuant to exercise of the Cure Option) within 20 days after the same shall become due or demanded, as the case may be; or

(ii) the Lessee shall fail to perform or observe any covenant, condition or agreement to be performed or observed by it under Section 10(b)(3)(i) or 10(b)(3)(ii) of the Participation Agreement or Section 7 or 11 of this Facility Lease; or

(iii) the Lessee shall fail to perform its agreements set forth in Section 5; or

(iv) the Lessee shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 10(b)(3)(v) of the Participation Agreement and such failure shall continue for a period of 15 days after there shall have been given to the Lessee by the Lessor or the Equity Participant

a notice specifying such failure and requiring it to be remedied and stating that such notice is a Notice of Default hereunder; or

(v) the Lessee shall fail to perform or observe any covenant, condition or agreement (other than those referred to in clauses (i) through (iv) above) to be performed or observed by it under this Facility Lease (other than Section 10) or any other Transaction Document; and such failure shall continue for a period of 30 days after there shall have been given to the Lessee by the Lessor or the Equity Participant a notice specifying such failure and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder; or

(vi) any representation or warranty made by the Lessee in this Facility Lease, any other Transaction Document (other than the Tax Indemnification Agreement) or any agreement, document or certificate delivered by the Lessee in connection herewith or therewith (other than in Section 7(b)(4) of the Participation Agreement) shall prove to have been incorrect in any material respect when any such representation or warranty was made or given and shall remain material and materially incorrect at the time in question; or

(vii) the Lessee shall commence a voluntary case or other proceeding seeking liquidation, reorganization or other relief with respect to itself or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, or shall consent to any such relief or to the appointment of or taking of possession by any such official in an involuntary case or other proceeding commenced against it, or shall make a general assignment for the benefit of creditors, or shall take any corporate action to authorize any of the foregoing; or an involuntary case or other proceeding shall be commenced against the Lessee seeking liquidation, reorganization

or other relief with respect to it or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, and such involuntary case or other proceeding shall remain undismissed or unstayed for a period of 60 consecutive days; or

(viii) final judgment for the payment of money in excess of \$10,000,000 shall be rendered against the Lessee and the Lessee shall not have discharged the same or provided for its discharge in accordance with its terms or bonded the same or procured a stay of execution thereof within 60 days from the entry thereof; or

(ix) (1) a default by the Lessee under the ANPP Participation Agreement in consequence of which the Lessee's right to receive its Generation Entitlement Share is suspended by the other ANPP Participants or (2) the giving by any ANPP Participant of a notice under Section 23.2 (or any comparable successor provision) of the ANPP Participation Agreement respecting a default thereunder by the Lessee and the lapse of 15 Business Days from the giving of such notice without the Lessee having cured such default; provided, however, that for purposes of this clause (2) if the Lessee shall have disputed the existence or nature of a default and such dispute shall have become the subject of an arbitration under Section 24 (or any comparable successor provision) of the ANPP Participation Agreement, such 15 Business Day period shall commence on the date of the final determination of the board of arbitrators under such provision; or

(x) (1) the Lessee shall fail to pay when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) any Debt of the Lessee the principal amount (or equivalent) of which is greater than \$20,000,000), and such failure shall continue

after the applicable grace period, if any, specified in the agreement or instrument relating to such Debt; or (2) any other default under any agreement or instrument relating to any such Debt, or any other event, shall occur and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such default or event is to accelerate the maturity of such Debt; or

(xi) the Lessee (A) shall fail, at any time, to provide or maintain a Letter of Credit which complies with all of the terms and conditions of Section 10(b) (3)(ix) of the Participation Agreement or (B) shall fail to provide a renewal or replacement Letter of Credit so complying (1) not less than 30 days prior to the stated termination date of an existing Letter of Credit, (2) within 20 days after the receipt by the Lessor of notice that an existing Letter of Credit will be terminated prior to its stated termination date under circumstances in which at least 30 days' notice of such termination is required or (3) concurrently with the receipt by the Lessor of notice that an existing Letter of Credit will be terminated prior to its stated termination date under circumstances in which less than 30 days' notice of such termination is required.

SECTION 16. Remedies.

(a) Remedies. Upon the occurrence of any Event of Default and so long as the same shall be continuing, the Lessor may, to the extent permitted by Applicable Law, exercise one or more of the following remedies, except as hereinbelow expressly otherwise set forth, as the Lessor in its sole discretion shall elect:

(i) the Lessor may declare this Facility Lease to be in default by written notice to such effect given to the Lessee, or may, by notice to the Lessee, rescind or terminate this Facility Lease;

(ii) the Lessor may (x) demand that the Lessee, and thereupon the Lessee shall, return possession of the Undivided Interest and the

Real Property Interest promptly to the Lessor in the manner and condition required by, and otherwise in accordance with the provisions of, this Facility Lease as if the Undivided Interest and the Real Property Interest were being returned at the end of the Lease Term, and the Lessor shall not be liable for the reimbursement of the Lessee for any costs and expenses incurred by the Lessee in connection therewith or (y) enter upon the PVNGS Site and take immediate possession of (to the exclusion of the Lessee) the Undivided Interest and the Real Property Interest, by summary proceedings or otherwise, all without liability to the Lessee for or by reason of such entry or taking of possession, whether for the restoration of damage to property caused by such taking or otherwise;

(iii) the Lessor may sell the Undivided Interest and the Real Property Interest, or any part thereof, together with any interest of the Lessor under the Assignment and Assumption or in respect of the Real Property Interest, at public or private sale, as the Lessor may determine, free and clear of any rights of the Lessee and without any duty to account to the Lessee with respect to such action or inaction or any proceeds with respect thereto (except to the extent required by clause (v) or (vi) below if the Lessor shall elect to exercise its rights thereunder), in which event the Lessee's obligation to pay Basic Rent hereunder for periods commencing after the date of such sale shall be terminated or proportionately reduced, as the case may be (except to the extent that Basic Rent is to be included in computations under clause (v) or (vi) below if the Lessor shall elect to exercise its rights thereunder);

(iv) the Lessor may hold, keep idle or lease to others all or any part of the Undivided Interest and the Real Property Interest, as the Lessor in its sole discretion may determine, free and clear of any rights of the Lessee and without any duty to account to the Lessee with respect to such action or

inaction or for any proceeds with respect to such action or inaction, except that the Lessee's obligation to pay Basic Rent for periods commencing after the Lessee shall have been deprived of use of the Undivided Interest and the Real Property Interest pursuant to this clause (iv) shall be reduced by an amount equal to the net proceeds, if any, received by the Lessor from leasing the Undivided Interest and the Real Property Interest to any Person other than the Lessee for the same periods or any portion thereof;

(v) except in the case of an Event of Default specified in clause (iii) of Section 15 (subject, however, to the proviso to the first sentence of Section 16(c) hereof), the Lessor may, whether or not the Lessor shall have exercised or shall thereafter at any time exercise its rights under clause (i), (ii), (iii) or (iv) above, demand, by written notice to the Lessee specifying a payment date which shall be a Basic Rent Payment Date not earlier than 10 days after the date of such notice, that the Lessee pay to the Lessor, and the Lessee shall pay to the Lessor, on the Basic Rent Payment Date specified in such notice, as liquidated damages for loss of a bargain and not as a penalty (in lieu of the Basic Rent due after the Basic Rent Payment Date specified in such notice), any unpaid Rent due through the Basic Rent Payment Date specified in such notice plus whichever of the following amounts the Lessor, in its sole discretion, shall specify in such notice together with interest on such amount at the interest rate specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice to the date of actual payment):

(A) an amount equal to the excess, if any, of (1) Casualty Value, computed as of the Basic Rent Payment Date specified in such notice, over (2) the Fair Market Rental Value of the Undivided Interest (determined on the basis of the then actual condition of Unit 2) until the end of the remaining useful life of

Unit 2, after discounting such Fair Market Rental Value semi-annually to present value as of the Basic Rent Payment Date specified in such notice at a rate of 10% per annum;

(B) an amount equal to the excess, if any, of (1) such Casualty Value over (2) the Fair Market Sales Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) as of the Basic Rent Payment Date specified in such notice; or

(C) an amount equal to the excess, if any, of (1) the present value as of the Basic Rent Payment Date specified in such notice of all installments of Basic Rent until the end of the Basic Lease Term or the Renewal Term, as the case may be, discounted semiannually at a rate of 10% per annum, over (2) the present value as of such Basic Rent Payment Date of the Fair Market Rental Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) until the end of the Basic Lease Term or the Renewal Term, as the case may be, discounted semiannually at a rate of 10% per annum;

(D) an amount equal to the highest of (1) such Casualty Value, (2) such discounted Fair Market Rental Value and (3) such Fair Market Sales Value and, in this event, upon full payment by the Lessee of all sums due hereunder, the Lessor shall, at its option, either Transfer the Undivided Interest and the Real Property Interest to the Lessee, or promptly sell the Undivided Interest and the Real Property Interest and pay over to the Lessee the net proceeds thereof up to the amount set forth in (1), (2) or (3) above actually paid by the Lessee to the Lessor;

(vi) if the Lessor shall have sold all the Undivided Interest and the Real Property Interest pursuant to clause (iii) above, the Lessor, in lieu of exercising its rights under clause (v) above, may, if it shall so elect, except in the case of an Event of Default specified in clause (iii) of Section 15, demand that the Lessee pay to the Lessor and the Lessee shall pay to the Lessor on the date of such sale, as liquidated damages for loss of a bargain and not as a penalty (in lieu of Basic Rent due for periods commencing after the next Basic Rent Payment Date following the date of such sale), any unpaid Basic Rent due through such Basic Rent Payment Date, plus the amount of any deficiency between the Sale Proceeds and Casualty Value, computed as of such Basic Rent Payment Date, together with interest at the interest rate specified in Section 3(b)(iii) on the amount of such Rent and such deficiency from the date of such sale until the date of actual payment;

(vii) in the case of an Event of Default specified in paragraph (iii) of Section 15, the Lessor may demand, by written notice to the Lessee that the Lessee pay to the Lessor, and the Lessee shall pay to the Lessor, on the last Basic Rent Payment Date during the Lease Term, as liquidated damages for loss of a bargain and not as a penalty, any unpaid Rent due through such Basic Rent Payment Date plus an amount (not less than zero) equal to the Fair Market Sales Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) determined as of such Basic Rent Payment Date together with interest on such amount at the interest rate specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice to the date of actual payment (and upon receipt of such payment the Lessor shall (or may prior to the receipt of such payment) Transfer to the Lessee the Undivided Interest and the Real Property Interest); provided, however, that the Lessor may not exercise the foregoing remedy if the Lessor shall have failed to Transfer the Undivided Interest and the Real

Property Interest to the bidder (which shall not be the Lessee or an Affiliate of the Lessee or any agent of any thereof) that shall have submitted the highest cash bid on or after the date two years before and on or before the date on which such Event of Default arose, excluding, however, any such cash bid which the Lessor or the Equity Participant determines was not submitted in good faith, or as to which the bidder fails to certify to the Lessor such information as the Lessor or Equity Participant may reasonably request in order to determine whether or not such bid was submitted in good faith (and the Lessor agrees that it will, if and to the extent so requested by the Lessee on or after the date 90 days preceding such last Basic Rent Payment Date, use reasonable efforts (at the expense of the Lessee) to find a Person willing to submit such cash bid; provided, however, that the failure of the Lessor to do so shall not relieve the Lessee of its obligations under this clause (vii)); or

(viii) except in the case of an Event of Default specified in clause (iii) of Section 15, the Lessor may exercise any other right or remedy that may be available to it under any Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(b) No Release. No rescission or termination of this Facility Lease, in whole or in part, or repossession of the Undivided Interest and the Real Property Interest or exercise of any remedy under Section 16(a) shall, except as specifically provided therein, relieve the Lessee of any of its liabilities and obligations hereunder. In addition, the Lessee shall be liable, except as otherwise provided above, for any and all unpaid Rent due hereunder before, after or during the exercise of any of the foregoing remedies, including all reasonable legal fees and other costs and expenses incurred by the Lessor, the Equity Participant or the Indenture Trustee by reason of the occurrence of any Event of Default or the exercise of the Lessor's remedies with respect thereto. At any sale of the Undivided Interest and the Real Property Interest or any part thereof pursuant to this Section 16, the Equity

Participant, the Lessor or the Indenture Trustee may bid for and purchase such property.

(c) Remedies Cumulative. Except as expressly set forth therein, no remedy under Section 16(a) is intended to be exclusive, but each shall be cumulative and in addition to any other remedy provided under Section 16(a) or otherwise available to the Lessor at law or in equity (except that the maximum amount payable by the Lessee in the event of the exercise by the Lessor of any of the remedies provided for in Section 16(a)(v) or (vi) shall not exceed the total amount payable by the Lessee under Section 16(a)(vii) minus the amount provided in subclause (2) of clause (A), (B) or (C) of such Section 16(a)(v), if the Lessor elects a remedy specified in said clause (A), (B) or (C), or the deficiency referred to in Section 16(a)(vi), if the Lessor elects the remedy specified in Section 16(a)(vi) hereof). No express or implied waiver by the Lessor of any Default or Event of Default hereunder shall in any way be, or be construed to be, a waiver of any future or subsequent Default or Event of Default. The failure or delay of the Lessor in exercising any right granted it hereunder upon the occurrence of any of the contingencies set forth herein shall not constitute a waiver of any such right upon the continuation or recurrence of any such contingencies or similar contingencies and any single or partial exercise of any particular right by the Lessor shall not exhaust the same or constitute a waiver of any other right provided herein. To the extent permitted by Applicable Law, the Lessee hereby waives any rights now or hereafter conferred by statute or otherwise which may require the Lessor to sell, lease or otherwise use the Undivided Interest or the Real Property Interest in mitigation of the Lessor's damages as set forth in Section 16(a) or which may otherwise limit or modify any of the Lessor's rights and remedies provided in this Section 16.

(d) Exercise of Other Rights or Remedies. In addition to all other rights and remedies provided in this Section 16, the Lessor may exercise any other right or remedy that may be available to it under Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(e) Special Cure Right of Lessee. If a Notice of Default is given under paragraph (iv) of Section 15,

the Lessee may, on or prior to the occurrence of an Event of Default resulting therefrom, give written notice to the Lessor stating that the Lessee has elected to exercise the option (the Cure Option) provided in this Section 16(e), which election shall be irrevocable as to the Lessee. Promptly after the giving of such notice, the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest and the Real Property Interest or, if they shall be unable so to agree within one month after the date of the Lessee's notice, such value shall be determined by the Appraisal Procedure. On the Basic Rent Payment Date next following the date that such Fair Market Sales Value shall have been determined, the Lessee shall pay to the Lessor all Rent due on such Basic Rent Payment Date, plus an amount equal to the excess of (i) the greater of such Fair Market Sales Value and the Casualty Value determined as of such Basic Rent Payment Date over (ii) the unpaid principal amount of the Notes Outstanding on such date after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of the Notes on such date. If the Lessee shall have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture, the Lessor shall Transfer the Undivided Interest to the Lessee. If the Lessee shall have made such payment but shall not have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture, the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount payable on each Basic Rent Payment Date thereafter equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law. The Lessee agrees to use its best efforts to comply with the conditions set forth in Section 3.9(b) of the Indenture and, failing such assumption, agrees to accept the Special Transfer.

(f) Offset for Drawings Under Letter of Credit. To the extent there has been an Event of Default under clause (xi) of Section 15 and no Event of Default under any other clause of such Section has occurred and

is continuing, any amount payable in respect of, or with reference to, Casualty Value as provided in this Section shall be reduced by any amount paid under the Letter of Credit in respect of such amount after the occurrence of such Event of Default.

SECTION 17. Notices.

All communications and notices provided for in this Facility Lease shall be in writing and shall be given in person or by means of telex, telecopy, or other wire transmission, or mailed by registered or certified mail, addressed as provided in the Participation Agreement. All such communications and notices given in such manner shall be effective on the date of receipt of such communication or notice.

SECTION 18. Successors and Assigns.

This Facility Lease, including all agreements, covenants, indemnities, representations and warranties, shall be binding upon and inure to the benefit of the Lessor and its successors and permitted assigns, and the Lessee and its successors and, to the extent permitted hereby, assigns.

SECTION 19. Right to Perform for Lessee.

If the Lessee shall fail to make any payment of Rent to be made by it, or shall fail to perform or comply with any of its other agreements contained herein, or shall fail to make any payment to be made by it under any ANPP Project Agreement, or shall fail to perform or comply with any of its other agreements contained in any ANPP Project Agreement, either the Lessor or the Equity Participant may, but shall not be obligated to, (i) to the extent not prohibited by Applicable Law tender such payment, or (ii) to the extent not prohibited by Applicable Law and, in the case of the ANPP Project Agreements, to the extent not expressly prohibited thereby, the ANPP Project Agreements, effect such performance or compliance, and the amount of such payment and the amount of all costs and expenses (including, without limitation, attorneys' and other professionals' fees and expenses) of the Lessor or the Equity Participant, as the case may be, incurred in connection with such payment or the performance of or compliance with such agreement, as the case may be, together with interest thereon at the higher of the

Overdue Interest Rate and the Penalty Rate, shall be deemed Supplemental Rent, payable by the Lessee upon demand. In the event that the Lessor or the Equity Participant shall cure any default by the Lessee under the ANPP Participation Agreement, then (so long as an Event of Default has occurred and is continuing) the Lessor, together with each other Person contributing to such cure, shall be entitled (to the full extent enforceable in accordance with Applicable Law and the ANPP Project Agreements) to receive the Generation Entitlement Share of the Lessee under the ANPP Participation Agreement (not limited to Unit 2), with each contributor to such cure to receive a percentage of such Generation Entitlement Share equal to the percentage of the cure contributed thereby.

SECTION 20. Additional Covenants.

The Lessee agrees to comply with and to pay, as Supplemental Rent, all amounts payable by it under the provisions of Section 13 of the Participation Agreement and the Tax Indemnification Agreement which provisions are incorporated herein by this reference as fully as if set forth in full at this place. The Lessee agrees to comply with its covenants and agreements set forth in Sections 10(b), 14 and 16 of the Participation Agreement and Articles III, IV, V and VI of the Assignment and Assumption, which covenants and agreements are incorporated herein by this reference as fully as if set forth in full at this place.

SECTION 21. Lease of Real Property Interest.

Pursuant to the Deed and the Assignment of Beneficial Interest, the Lessee has sold to the Lessor the Real Property Interest. The Lessor hereby grants to the Lessee a leasehold interest in the Real Property Interest, such leasehold to be coterminous with the lease of the Undivided Interest hereunder and to be at a rent per annum equal to 12% of the Real Estate Investment payable by the Lessee to the Lessor in arrears in equal semiannual installments on each Basic Rent Payment Date during the Lease Term.

SECTION 22. Amendments and Miscellaneous.

(a) Amendments in Writing. The terms of this Facility Lease may not be waived, altered, modified, amended, supplemented or terminated in any manner whatsoever except by written instrument signed by the Lessor and the Lessee.

(b) Survival. (1) All indemnities, representations and warranties contained in this Facility Lease and the other Transaction Documents and any Financing Documents and in any agreement, document or certificate delivered pursuant hereto or thereto or in connection herewith or therewith shall survive, and continue in effect following, the execution and delivery of this Facility Lease and the expiration or other termination of this Facility Lease.

(2) The obligations of the Lessee to pay Supplemental Rent and the obligations of the Lessee under Sections 5, 16, 19 and 20 shall survive the expiration or termination of this Facility Lease. The modification by law of any statute of limitations or the waiver or extension of any statute of limitations by the Owner Trustee, the Indenture Trustee, the Lessee, the Equity Participant, the Loan Participant or any Indemnatee shall not affect such survival. The obligations of the Lessee under Section 20 are expressly made for the benefit of, and shall be enforceable by, any Indemnatee, separately or together, without declaring this Facility Lease to be in default and notwithstanding any assignment by the Lessor of this Facility Lease or any of its rights thereunder or any disposition of all or any part of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Facility Lease or in this Facility Lease or any other Transaction Document or Financing Document. All payments required to be made pursuant to Section 20 shall be made directly to, or as otherwise requested by, the Indemnatee entitled thereto upon written demand by such Indemnatee.

(c) Severability of Provisions. Any provision of this Facility Lease which may be prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof or thereof, and any such prohibition or unenforceability in any jurisdiction

shall not invalidate or render unenforceable such provision in any other jurisdiction. To the extent permitted by Applicable Law, the Lessee hereby waives any provision of law which renders any provision hereof prohibited or unenforceable in any respect.

(d) True Lease. This Facility Lease is intended as and shall constitute an agreement of lease and nothing herein shall be construed as conveying to the Lessee any right, title or interest in or to the Undivided Interest or the Real Property Interest, except as lessee only.

(e) Original Lease. The single executed original of this Facility Lease marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART" and containing the receipt of the Indenture Trustee thereon shall be the Original of this Facility Lease. To the extent that this Facility Lease constitutes chattel paper, as such term is defined in the Uniform Commercial Code as in effect in any applicable jurisdiction, no security interest in this Facility Lease may be created through the transfer or possession of any counterpart other than the Original.

(f) Governing Law. This Facility Lease shall be governed by and construed in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

(g) Headings. The division of this Facility Lease into sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Facility Lease.

(h) Concerning the Owner Trustee. FNB is entering into this Facility Lease solely as Owner Trustee under the Trust Agreement and not in its individual capacity. Anything herein to the contrary notwithstanding, all and each of the representations, warranties, undertakings and agreements herein made on the part of the Owner Trustee are made and intended not as personal representations, warranties, undertakings and agreements by or for the purpose or with the intention of binding FNB personally but are made and intended for the purpose of binding only the Trust Estate, and this Facility Lease is executed and delivered by the Owner Trustee solely in the exercise of the powers expressly

conferred upon it as trustee under the Trust Agreement; and no personal liability or responsibility is assumed hereunder by or shall at any time be enforceable against FNB or any successor in trust or the Equity Participant on account of any representation, warranty, undertaking or agreement hereunder of the Owner Trustee, either expressed or implied, all such personal liability, if any, being expressly waived by the Lessee, except that the Lessee or any Person claiming by, through or under it, making claim hereunder, may look to the Trust Estate for satisfaction of the same and the Owner Trustee or its successor in trust, as applicable, shall be personally liable for its own gross negligence or willful misconduct. If a successor owner trustee is appointed in accordance with the terms of the Trust Agreement, such successor owner trustee shall, without any further act, succeed to all the rights, duties, immunities and obligations of the Owner Trustee hereunder and the predecessor owner trustee shall be released from all further duties and obligations hereunder.

(i) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Finance Co., a Delaware corporation, whose address is 111 East Prospect, Stamford, CT 06904: Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

(j) Capacity of Lessee. In addition to being an ANPP Participant, APS is also the Operating Agent for PVNGS. The Lessor understands and agrees that APS has certain duties and responsibilities as such Operating Agent under Applicable Law, as well as to the ANPP Participants under the ANPP Project Agreements, and that the obligations of the Lessee hereunder shall not be interpreted as imposing any additional obligation on APS as a result of its status as Operating Agent.

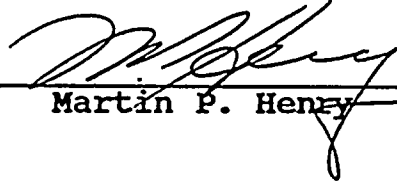
(k) Lien of Lease Indenture. The Lessee hereby agrees that any transfer of all or any part of the property which is subject to the lien of the Indenture, to the extent such lien cannot be released, shall be transferred subject to such lien.

(l) Counterpart Execution. This Facility Lease may be executed in any number of counterparts and by

each of the parties hereto or thereto on separate counterparts, all such counterparts together constituting but one and the same instrument.

IN WITNESS WHEREOF, each of the parties hereto has caused this Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement dated as of August 1, 1986, with Emerson Finance Co.

By 
Martin P. Henry

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Paul A. Williams II

IN WITNESS WHEREOF, each of the parties hereto has caused this Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement dated as of August 1, 1986, with Emerson Finance Co.

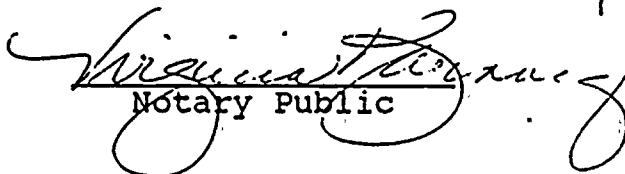
By _____
Martin P. Henry

ARIZONA PUBLIC SERVICE
COMPANY

By  _____
Paul A. Williams II

State of New York)
) ss:
County of New York)

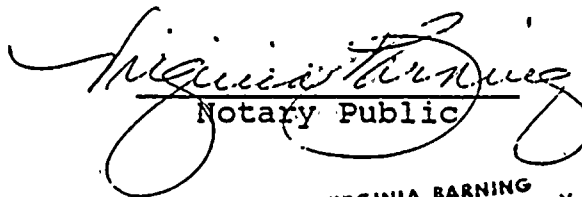
The foregoing instrument was acknowledged before me this 18th day of August, 1986, by PAUL A. WILLIAMS II, the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of said corporation.


Notary Public

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified in Kings County
Certificate filed in New York County
Commission Expires March 30, 1988

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by MARTIN P. HENRY, an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as trustee under that certain Trust Agreement, dated as of August 1, 1986, with Emerson Finance Co..


Notary Public

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified in Kings County
Certificate filed in New York County
Commission Expires March 30, 1988

When Recorded, Return to: David A. Sprentall
SNELL & WILMER
3100 Valley Bank Center
Phoenix, Arizona 85073

CERTAIN RIGHTS OF THE LESSOR UNDER THE FACILITY LEASE AS AMENDED BY THIS AMENDMENT NO. 1 THERETO HAVE BEEN ASSIGNED TO, AND ARE SUBJECT TO A SECURITY INTEREST IN FAVOR OF, CHEMICAL BANK, AS INDENTURE TRUSTEE UNDER A TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE-DATED AS OF AUGUST 1, 1986. THIS AMENDMENT NO. 1 HAS BEEN EXECUTED IN SEVERAL COUNTERPARTS. SEE SECTION 3(d) OF THIS AMENDMENT NO. 1 FOR INFORMATION CONCERNING THE RIGHTS OF HOLDERS OF VARIOUS COUNTERPARTS HEREOF.

THIS COUNTERPART IS NOT THE ORIGINAL COUNTERPART.

AMENDMENT NO. 1
dated as of November 1, 1986

to

FACILITY LEASE
dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON
not in its individual capacity, but solely
as Owner Trustee under a Trust Agreement
dated as of August 1, 1986 with Emerson
Capital Corporation (assignee of Emerson
Finance Co.)

Lessor .

and

ARIZONA PUBLIC SERVICE COMPANY,

Lessee

Original Facility Lease Recorded on August 18, 1986,
as Instrument No. 86-439438 in Maricopa County,
Arizona Recorder's Office.

AMENDMENT NO. 1, dated as of November 1, 1986 (Amendment No. 1), to the Facility Lease dated as of August 1, 1986 between THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement, dated as of August 1, 1986, with Emerson Capital Corporation, a Delaware corporation, as assignee of Emerson Finance Co. (the Lessor), and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee):

W I T N E S S E T H :

WHEREAS, the Lessee and the Lessor have heretofore entered into a Facility Lease dated as of August 1, 1986 (the Facility Lease), providing for the lease by the Lessor to the Lessee of the Undivided Interest and the Real Property Interest;

WHEREAS, Section 3(d) of the Facility Lease provides for an adjustment to Basic Rent and to the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event of a Change in Tax Law;

WHEREAS, Section 3(e) of the Facility Lease provides for an adjustment to Basic Rent and to the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event, among other things, of the refunding, by issuance of the Refunding Notes, of the Initial Series Notes; and

WHEREAS, the Refunding Notes are being issued pursuant to Supplemental Indenture No. 1, dated as of November 1, 1986, to the Indenture;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein and not otherwise defined herein or in the recitals shall have the meanings assigned to such terms in Appendix A hereto.

SECTION 2. Amendments.

(a) The second WHEREAS clause of the Facility Lease is amended hereby by inserting the clause "and the Real Property Interest" in such WHEREAS clause after the first use of the term "Undivided Interest".

(b) Section 3(a)(i) of the Facility Lease is amended hereby to read in its entirety as follows:

"(i) on December 30, 1986, an amount equal to the daily equivalent of Basic Rent (which, for the entire period from and including August 18, 1986 to but excluding December 31, 1986, is set forth in Schedule 1 hereto) plus or minus any Rent Differential for the period from the Closing Date to and including December 31, 1986;"

(c) Section 3(a)(ii) of the Facility Lease is amended hereby to read in its entirety as follows:

"(ii) on June 30, 1987 and on each Basic Rent Payment Date thereafter to and including December 30, 2015, an amount equal to the percentage of Facility Cost set forth opposite such Basic Rent Payment Date in Schedule 1 hereto;"

(d) Section 3(a)(iv) of the Facility Lease is amended hereby by replacing the phrase "a Fair Market Renewal Term" with the phrase "the Fair Market Renewal Term" in Section 3(a)(iv).

(e) Section 3(a) of the Facility Lease is amended hereby by amending the clause "such Rent Payment Date" in the penultimate sentence of Section 3(a) to read "such Basic Rent Payment Date" and by amending the last sentence of Section 3(a) in its entirety to read as follows:

"If an interest payment on any Note shall be due on a date other than December 30, 1986 or a Basic Rent Payment Date, the Lessee shall pay Basic Rent on such date equal to such interest payment and such payment of Basic Rent shall be credited against the Basic Rent due on December 30, 1986 or the Basic Rent Payment Date next succeeding the date that such additional Basic Rent shall have been paid."

(f) Section 3(b)(ii) of the Facility Lease is amended hereby by deleting the word "hereunder" from Section 3(b)(ii).

(g) Section 3(e) of the Facility Lease is amended hereby by (i) adding the word "Current" before the phrase "Pricing Assumptions" in the first sentence of Section 3(e) and (ii) by deleting the phrase "hereof also" in the second sentence of Section 3(e).

(h) Section 3(f) of the Facility Lease is amended hereby by (i) replacing the phrase "Sections 3(d) or (e)" with the phrase "Section 3(d) or (e)" in the first sentence of Section 3(f), (ii) replacing the phrase "any Loan Participant" with the phrase "each Loan Participant" in the first sentence of Section 3(f), (iii) replacing the phrase "bank which has issued the Letter of Credit" with the phrase "issuer of the Letter of Credit" in the first sentence of Section 3(f) and (iv) amending the third sentence of Section 3(f) to read in its entirety as follows:

"The revised amounts and percentages, as so confirmed or computed if applicable, shall be

conclusive and binding on the Lessee, the Lessor, the Equity Participant, each Loan Participant, the Indenture Trustee and the Collateral Trust Trustee."

(i) Section 3(g) of the Facility Lease is amended hereby by replacing the parenthetical "(when added to all other amounts required to be paid by the Lessee under this Facility Lease in respect of any Event of Loss or Deemed Loss Event or termination of this Facility Lease)" in clause (ii) of Section 3(g) with the parenthetical "(when added to all other amounts required to be paid by the Lessee in respect of any Event of Loss or Deemed Loss Event or purchase by the Lessee of the Undivided Interest or termination of this Facility Lease)".

(j) Section 3(h) of the Facility Lease is hereby amended to read in its entirety as follows:

"(h) Rent Differential. The installment of Basic Rent payable on December 30, 1986 shall be increased or decreased, as the case may be, by the Rent Differential. For purposes hereof, "Rent Differential" shall mean the difference between (i) the aggregate amount of interest paid on the Initial Series Notes and (ii) \$3,167,275.40. If (A) the amount determined in accordance with clause (i) of the immediately preceding sentence shall exceed the amount set forth in clause (ii) of such sentence, the amount of Basic Rent due on such date shall be increased by the Rent Differential, and (B) the amount set forth in such clause (ii) shall exceed the amount determined in accordance with such clause (i), the amount of Basic Rent due on such date shall be decreased by the Rent Differential."

(k) Section 5(a) of the Facility Lease is amended hereby in its entirety to read as follows:

"SECTION 5. Return of the Undivided Interest;
Disposition Services.

"(a) Return of the Undivided Interest. Unless the Lessee has acquired the Undivided Interest and the Real Property Interest as provided herein, on the Lease Termination Date, the Lessee will surrender possession of the Undivided Interest and the Real Property Interest to the Lessor (or to a Person specified by the Lessor to the Lessee in writing not less than 6 months prior to the Lease Termination Date) with full rights as a 'Transferee' and the sole 'Participant' with respect to the Undivided Interest and the Real Property Interest within the meaning of Section 15.10 of the ANPP Participation Agreement, and will furnish to the Lessor: (i) copies certified by a senior officer of the Lessee of all Governmental Actions necessary to effect such surrender (including, without limitation, appropriate amendments to the License permitting the Lessor (without being required to change its business or corporate structure) and for such Person to possess the Undivided Interest and the Real Property Interest without the continued involvement of the Lessee), which Governmental Actions shall be in full force and effect and not subject to any judicial or administrative contest, challenge or review; (ii) if not previously executed and delivered by the Lessee, and if desired by the Lessor, a ground lease covering that portion of the PVNGS Site which is included in the Real Property Interest, which ground lease shall have a term ending on the date of reversion of the Real Property Interest and shall be otherwise reasonably satisfactory to the Lessor, in replacement for the Real Property Interest; and (iii) an opinion of counsel (which may be Mudge Rose Guthrie Alexander & Ferdon, Snell & Wilmer or other counsel experienced in matters

pertaining to the Governmental Actions required, reasonably satisfactory to the Equity Participant) to the effect that (A) the Lessee has obtained all Governmental Actions and actions under the ANPP Participation Agreement necessary to effect such surrender by the Lessee and receipt of possession by the Lessor (or the Person so specified by the Lessor) of the Undivided Interest and the Real Property Interest, (B) the Lessor (or the Person specified by the Lessor) is a NRC Licensee and an ANPP Participant (with all rights and obligations attendant thereto) and no additional Governmental Action will be required in connection with the possession by the Lessor (or the Person specified by the Lessor) of the Undivided Interest and the Real Property Interest, (C) such Governmental Actions are in full force and effect and not subject to any judicial or administrative contest, challenge or review and (D) to the extent the aforementioned ground lease is required, such ground lease (1) has been duly authorized, executed and delivered, (2) constitutes the legal, valid and binding obligation of the Lessee, (3) does not require the consent of any Person or such consent has been previously received and (4) is not inconsistent with any ANPP Project Agreement. At the time of such return the Lessee shall pay or have paid all amounts due and payable, or to become due and payable, by it as an ANPP Participant under each and every ANPP Project Agreement allocable or chargeable (whether or not payable during or after the Lease Term) to the Undivided Interest or the Real Property Interest in respect of any period or periods ending on or prior to the Lease Termination Date (including, without limitation, all amounts payable with respect to any and all Capital Improvements to Unit 2 or the PVNGS Site approved or authorized (without the concurrence of the Equity Participant) prior

to the end of the Lease Term, whether or not implementation thereof has been completed on or prior to the Lease Termination Date), and the Undivided Interest and the Real Property Interest shall be free and clear of all Liens (other than Permitted Liens described in clauses (i), (v) (other than those for which satisfactory arrangements for the payment thereof have not been made and those arising by, through or under the Lessee alone), (vi), (vii) (other than those arising by, through, or under the Lessee alone), (ix) or (x) of the definition of such term) and in the condition and state of repair required by Section 8. In the event that on or prior to the Lease Termination Date there shall have occurred a default by any ANPP Participant (other than the Lessee) under the ANPP Participation Agreement and such default shall not have been cured by the defaulting ANPP Participant, then (x) the Lessee agrees to indemnify and hold the Lessor (and each successor, assign and transferee thereof) harmless against any and all obligations under the ANPP Participation Agreement with respect to contributions or payments required to be made thereby as a result of such default and (y) the Lessor (and each successor, assign and transferee thereof) agrees to reimburse the Lessee for all amounts paid by the Lessee pursuant to the foregoing clause (x) in respect of the period following the Lease Termination Date to the extent, but only to the extent, that the Lessor (or such successor, assign or transferee) shall have actually received net proceeds from the sale of the Generation Entitlement Share of the defaulting ANPP Participant as a result of the payment made by the Lessee pursuant to the foregoing clause (x), and, to the extent the Lessor (or such successor, assign or transferee) shall have received such proceeds, the amount to be reimbursed to the Lessee pursuant to this clause (y) shall include

interest at the Prime Rate from the date of any payment by the Lessee pursuant to the foregoing clause (x) through the date of reimbursement of such amount pursuant to this clause (y)."

(l) Section 8(c) of the Facility Lease is amended hereby by (i) replacing the phrase "The net proceeds" at the beginning of the fourth sentence of Section 8(c) with the phrase "With respect to the net proceeds" and (ii) replacing the seventh sentence of Section 8(c) to read as follows:

"Unless paragraph (3) of Section 8(e) shall be applicable, upon the incorporation of a Capital Improvement in Unit 2, without further act, title to the Unit 2 Interest in such Capital Improvement shall vest in the Lessor and shall become subject to this Facility Lease and be deemed to be part of the Undivided Interest for all purposes hereof to the same extent that the Lessor had a like undivided interest in the property originally incorporated or installed in Unit 2."

(m) Section 9(c) of the Facility Lease is amended hereby by replacing the phrase "On the date next following" in the first sentence of Section 9(c) with the phrase "On a date following".

(n) Section 9(c)(i) of the Facility Lease is amended hereby by (i) replacing the phrase "such ANPP Participant" in Section 9(c)(i) with the phrase "such ANPP Participants", (ii) replacing the phrase "right against the Lessee" in Section 9(c)(i) with the phrase "right against the Lessee)" and (iii) replacing the phrase "may appear;" in Section 9(c)(i) with the phrase "may appear;".

(o) Section 9(g)(ii) is amended hereby by deleting the parenthetical "(ignoring, for this purpose, clause (ii) of the first sentence thereof)".

(p) Section 9(h) of the Facility Lease is amended hereby by amending the clause "or the third sentence of Section 8(c), destruction" to read "or the fourth sentence of Section 8(c), or to any destruction" and by adding a comma after the phrase "constituting an Event of Loss".

(q) Section 10(a)(1)(i) of the Facility Lease is amended hereby by replacing the first sentence thereof as follows:

"(1) Non-Nuclear Insurance.

"(i) The Lessee shall maintain 'all risk' property insurance covering physical loss with respect to Unit 2 in such amounts and with such other terms as are required by or are in accordance with Prudent Utility Practice, but in no event shall such amounts be less than the estimated maximum probable loss in respect of such property."

(r) Section 10(a)(1)(i)(B) of the Facility Lease is amended to read as follows:

"(B)(i) the Lessor and the Equity Participant (the 'Additional Insureds') are included as additional insureds, as their interests may appear, and (ii) any obligation imposed upon the insured (including without limitation the liability to pay premiums) shall be the sole obligation of the Lessee and not that of any Additional Insured;"

(s) Section 10(a)(1)(ii) of the Facility Lease is amended hereby by adding the phrase "The Lessee shall

maintain" immediately after the "(ii)" and before the phrase "bodily injury".

(t) Section 10(a)(2) of the Facility Lease is amended hereby in its entirety to read as follows:

"(2) Nuclear Insurance.

"(i) The Lessee shall maintain nuclear property insurance in amounts and with such other terms as are required by or are in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement and (c) Prudent Utility Practice; provided, however, that such insurance shall at all times be maintained in amounts at least equal to the maximum nuclear property insurance available on commercially reasonable terms. The coverage afforded by such nuclear property insurance in respect of any loss at PVNGS and available for any loss at Unit 2 either (A) shall at all times be at least equal to \$750 million regardless of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of Nuclear Incident) or (B) so long as (1) Unit 2 is in, or is in a procedure which will result in, a state of cold shutdown in accordance with Prudent Utility Practice and (2) the first mortgage bonds of the Lessee shall have an investment grade rating (x) by two nationally accepted rating agencies if such first mortgage bonds are rated by two nationally accepted rating agencies or (y) by one nationally accepted rating agency if such first mortgage bonds are only rated by one nationally accepted rating agency, will be reinstated to be equal to at least \$750 million within 180 days of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of a Nuclear Incident). Such insurance may include deductible amounts not to exceed

\$10,000,000. Any insurance carried in accordance with this Section 10(a)(2)(i) shall be endorsed by the insurer as provided in paragraphs (A), (B), (D), (E) and (F) of Section 10(a)(1)(i).

"(ii) The Lessee shall maintain the maximum nuclear liability insurance in amounts and with such other terms as are required by or in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement, (c) Prudent Utility Practice and (d) the maximum nuclear liability insurance available on commercially reasonable terms, but in any event in such amounts and containing such other terms as to cover the 'aggregate liability' for a single 'nuclear incident' of all 'persons indemnified' (as such terms are used in the Atomic Energy Act) and in connection with the ownership, maintenance, condition or use of Unit 2 and the PVNGS Site. The Lessee shall also maintain supplier's and transporter's insurance in amounts consistent with Prudent Utility Practice. The Lessee shall maintain nuclear liability insurance pursuant to this Section 10(a)(2)(ii), whether or not the Lease Termination Date shall have occurred, until notified by the Equity Participant that neither the Lessor nor the Equity Participant has any further real or potential liability in connection with the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site; provided that after Decommissioning has been completed the Lessee shall not be required to maintain nuclear liability insurance for more than 30 years. Any insurance carried in accordance with this Section 10(a)(2)(ii) shall be endorsed as provided in paragraphs (B), (D), (E) and (F) of Section 10(a)(1)(i).

"(iii) The Lessee shall, or shall cause the Operating Agent to, use its best efforts

at all times to obtain the endorsement referred to in paragraph (C) of Section 10(a)(1)(i) on all insurance referred to in this Section 10 (a)(2), and shall cause such endorsement to be obtained if and to the extent it is available to any other owner or operator of a nuclear generating unit."

(u) Section 11(b) of the Facility Lease is hereby amended by amending the last sentence of Section 11(b) in its entirety to read as follows:

"Following any transfer to, or purchase by, Lessee of the Undivided Interest and the Real Property Interest, the Undivided Interest and the Real Property Interest shall (unless the Notes shall have been paid in full) remain subject to the lien of the Indenture and such lien shall not be impaired in consequence thereof."

(v) Section 12(b) of the Facility Lease is amended hereby in its entirety to read as follows:

"(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period of 6, 12, 18 or 24 months (herein referred to as the Fair Market Renewal Term; and the Fixed Rate Renewal Term (including any extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in

which case Basic Rent payable during such Fair Market Renewal Term shall be as set forth in Section 3(a)(iv)."

(w) Section 13(a) of the Facility Lease is amended hereby in its entirety to read as follows:

"(a) Expiration of Basic Lease Term. Not earlier than five nor later than three years prior to the expiration date of the Basic Lease Term, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(a) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration date of the Basic Lease Term, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fixed Rate Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor if, on the effective date thereof, a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(a), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant

shall be unable so to agree, such Fair Market Sales Value shall be determined by the Appraisal Procedure. In the case of the exercise of the option for the Fixed Rate Renewal Term, the Maximum Option Period shall be determined by the Appraisal Procedure."

(x) Section 13(b) of the Facility Lease is amended hereby in its entirety to read as follows:

"Expiration of Fixed Rate Renewal Term. Not earlier than five years nor later than three years prior to the expiration date of the Fixed Rate Renewal Term, if elected, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(b) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration of the Fixed Rate Renewal Term, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fair Market Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor, if, on the effective date thereof, a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(b), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value and the Fair

Market Rental Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such values shall be determined by the Appraisal Procedure."

(y) Section 13(c) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 13(c).

(z) Section 13(d) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in the heading and after the first use of the phrase "Undivided Interest" in the first sentence of Section 13(d).

(aa) Section 13(e) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 13(e).

(bb) Section 14(c) of the Facility Lease is amended hereby by (i) adding the phrase "and the Real Property Interest" after the two uses of the phrase "Undivided Interest" in the first sentence of Section 14(c), (ii) amending the second and third sentences of Section 14(c) in their entirety to read as follows:

"The total sale price realized at such sale shall be retained by the Lessor (subject, however, to the terms of the Indenture and the requirement that on the Termination Date there shall have been paid, or provision for payment made, to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on the Obsolescence Redemption Date and all premium, if any, and interest accrued and unpaid on such Outstanding Notes as of the Termination Date, and to accrue on such

Outstanding Notes to the Obsolescence Redemption Date) and, in addition, on the Termination Date the Lessee shall pay to the Lessor (A) the excess, if any, of the sum of the Special Casualty Value as of the Termination Date over the net sale price of the Undivided Interest and the Real Property Interest and (B) any Basic Rent due or accrued, as the case may be, to and including the Termination Date and an amount equal to any interest to accrue on the Outstanding Notes from and including the Termination Date to the Obsolescence Redemption Date, and shall pay to the Person or Persons entitled thereto all Supplemental Rent (other than Special Casualty Value). Upon compliance by the Lessee with the applicable provisions of this Section 14, the obligation of the Lessee to pay Basic Rent for any period after the Termination Date shall cease and the Basic Lease Terms shall end on the Termination Date but the obligation of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination."

and (iii) by adding the phrase "and the Real Property Interest" after the first use of the phrase "Undivided Interest" in the last sentence of Section 14.(c).

(cc) Section 15(xi) of the Facility Lease is amended hereby by replacing the term "Lessor" with the term "Equity Participant" each time such term is used in Section 15(xi).

(dd) Section 16(a)(v) of the Facility Lease is amended hereby by (i) replacing the phrase "proviso to" with the phrase "parenthetical in" in the first parenthetical clause of Section 16(a)(v), (ii) removing the parenthesis before the colon in the first paragraph of Section 16(a)(v), and (iii) adding the phrase "and the

Real Property Interest" after the phrase "Undivided Interest" in Section 16(v)(A).

(ee) Section 16(a)(vii) of the Facility Lease is amended hereby by replacing the clause "specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice" in Section 16(a)(vii) with the clause "specified in Section 3(b)(iii) from such last Basic Rent Payment Date".

(ff) Section 16(c) of the Facility Lease is amended hereby by amending the first sentence of Section 16(c) in its entirety to read as follows:

"Except as expressly set forth therein, no remedy under Section 16(a) is intended to be exclusive, but each shall be cumulative and in addition to any other remedy provided under Section 16(a) or otherwise available to the Lessor at law or in equity (except that, in the case of an Event of Default specified in clause (iii) of Section 15, the Lessor may not exercise any of the remedies provided for in Section 16(a)(v), 16(a)(vi) or 16(a)(viii))."

(gg) Section 16(e) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in the fourth sentence of Section 16(e) and by deleting the last sentence of Section 16(e).

(hh) Section 21 of the Facility Lease is amended hereby by deleting the phrase "and the Assignment of Beneficial Interest" from Section 21.

(ii) Section 22(b)(2) of the Facility Lease is amended hereby by replacing the phrase "the Loan Participant" in the second sentence of Section 22(b)(2) with the phrase "any Loan Participant".

(jj) The Facility Lease is amended hereby by replacing the phrase "any Collateral Trust Trustee" with

the phrase "the Collateral Trust Trustee" in each place in the Facility Lease where such phrase appears.

(kk) Appendix A to the Facility Lease is hereby deleted in its entirety and replaced with Appendix A hereto.

(ll) Schedule 1 to the Facility Lease is hereby replaced with Schedule 1 hereto.

(mm) Schedule 2 to the Facility Lease is hereby replaced with Schedule 2 hereto.

(nn) Schedule 3 to the Facility Lease is hereby replaced with Schedule 3 hereto.

(oo) Schedule 4 to the Facility Lease is hereby replaced with Schedule 4 hereto.

(pp) Schedule 5 to the Facility Lease is hereby replaced with Schedule 5 hereto.

(qq) The titles of Schedules 6 and 7 to the Facility Lease are hereby changed to "Description of Undivided Interest" and "Description of Real Property Interest", respectively.

(rr) Schedule 8 to the Facility Lease is hereby deleted.

SECTION 3. Miscellaneous.

(a) Dating. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Governing Law. This Amendment No. 1 has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York, except to the

extent that pursuant to the law of the State of Arizona such law is mandatorily applicable hereto.

(c) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Capital Corporation, a Delaware corporation. The address of the beneficiary is 8000 West Florissant Avenue, St. Louis, Missouri 63136, Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

(d) Original Counterpart. The single executed original of this Amendment No. 1 marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART" and containing the receipt of the Indenture Trustee thereon shall be the "Original" of this Amendment No. 1. No security interest in this Amendment No. 1 may be created or continued through the transfer or possession of any counterpart other than the "Original".

IN WITNESS WHEREOF, each of the parties hereto has caused this Amendment No. 1 to Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON,
not in its individual
capacity, but solely as
Owner Trustee under a Trust
Agreement dated as of
August 1, 1986, with
Emerson Capital Corporation
(assignee of Emerson
Finance Co.)

By



Martin P. Henry

Assistant Vice President

Date: November 19, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By


Paul A. Williams II

Vice President and Treasurer

Date: November 19, 1986

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under the Trust Agreement dated as of August 1, 1986 with Emerson Capital Corporation (assignee of Emerson Finance Co.).

Notary Public
Notary Public for the State of New York
Qualified in New York
Commission Expires March 30, 1986

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by PAUL A. WILLIAMS .II, Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.

Notary Public
Notary Public for the State of New York
Qualified in New York
Commission Expires March 30, 1986

SCHEDULE 1
to
AMENDMENT NO. 1

BASIC RENT PERCENTAGES

Basic Rent Payment Date	Basic Rent Number	% of Facility Cost	Basic Rent Payment Date	Basic Rent Number	% of Facility Cost
12 /30 /1986	0	3.6826923	12 /30 /2001	30	5.3757422
6 /30 /1987	1	4.3983345	6 /30 /2002	31	5.3757422
12 /30 /1987	2	4.3983345	12 /30 /2002	32	5.3757422
6 /30 /1988	3	4.3983345	6 /30 /2003	33	5.3757422
12 /30 /1988	4	4.3983345	12 /30 /2003	34	5.3757422
6 /30 /1989	5	4.3983345	6 /30 /2004	35	5.3757422
12 /30 /1989	6	4.3983345	12 /30 /2004	36	5.3757422
6 /30 /1990	7	4.3983345	6 /30 /2005	37	5.3757422
12 /30 /1990	8	4.3983345	12 /30 /2005	38	5.3757422
6 /30 /1991	9	4.3983345	6 /30 /2006	39	5.3757422
12 /30 /1991	10	4.3983345	12 /30 /2006	40	5.3757422
6 /30 /1992	11	4.3983345	6 /30 /2007	41	5.3757422
12 /30 /1992	12	4.3983345	12 /30 /2007	42	5.3757422
6 /30 /1993	13	4.3983345	6 /30 /2008	43	5.3757422
12 /30 /1993	14	4.3983345	12 /30 /2008	44	5.3757422
6 /30 /1994	15	4.3983345	6 /30 /2009	45	5.3757422
12 /30 /1994	16	4.3983345	12 /30 /2009	46	5.3757422
6 /30 /1995	17	4.3983345	6 /30 /2010	47	5.3757422
12 /30 /1995	18	4.3983345	12 /30 /2010	48	5.3757422
6 /30 /1996	19	4.3983345	6 /30 /2011	49	5.3757422
12 /30 /1996	20	4.3983345	12 /30 /2011	50	5.3757422
6 /30 /1997	21	4.3983345	6 /30 /2012	51	5.3757422
12 /30 /1997	22	5.3757422	12 /30 /2012	52	5.3757422
6 /30 /1998	23	5.3757422	6 /30 /2013	53	5.3757422
12 /30 /1998	24	5.3757422	12 /30 /2013	54	5.3757422
6 /30 /1999	25	5.3757422	6 /30 /2014	55	5.3757422
12 /30 /1999	26	5.3757422	12 /30 /2014	56	5.3757422
6 /30 /2000	27	5.3757422	6 /30 /2015	57	5.3757422
12 /30 /2000	28	5.3757422	12 /30 /2015	58	5.3757422
6 /30 /2001	29	5.3757422			

SCHEDULE 2
to
AMENDMENT NO. 1

CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Basic Rent Payment Date	Casualty Value	Basic Rent Payment Date	Casualty Value
-----	-----	-----	-----
6 /30 /1987	104.9360095	12 /30 /2001	96.7381114
and before		6 /30 /2002	94.8366249
12 /30 /1987	103.2818335	12 /30 /2002	92.8747085
6 /30 /1988	104.8235657	6 /30 /2003	90.8583110
12 /30 /1988	106.2364796	12 /30 /2003	88.7788264
6 /30 /1989	107.5243572	6 /30 /2004	86.6427680
12 /30 /1989	108.7048562	12 /30 /2004	84.4410832
6 /30 /1990	109.7593567	6 /30 /2005	82.1808790
12 /30 /1990	110.6918960	12 /30 /2005	79.8526142
6 /30 /1991	111.5025202	6 /30 /2006	77.4641357
12 /30 /1991	112.1912333	12 /30 /2006	75.0054079
6 /30 /1992	112.7525270	6 /30 /2007	72.4850582
12 /30 /1992	113.1945127	12 /30 /2007	69.8925658
6 /30 /1993	113.4999272	6 /30 /2008	67.2373951
12 /30 /1993	113.6666580	12 /30 /2008	64.5085576
6 /30 /1994	113.6759686	6 /30 /2009	61.7165153
12 /30 /1994	113.5240160	12 /30 /2009	58.8498025
6 /30 /1995	113.1903637	6 /30 /2010	55.9200097
12 /30 /1995	112.7898796	12 /30 /2010	52.9152047
6 /30 /1996	112.3737914	6 /30 /2011	49.8482183
12 /30 /1996	111.9415879	12 /30 /2011	46.7067242
6 /30 /1997	111.4927722	6 /30 /2012	43.5049350
12 /30 /1997	110.0494116	12 /30 /2012	40.2301802
6 /30 /1998	108.5444219	6 /30 /2013	36.9345433
12 /30 /1998	106.9905349	12 /30 /2013	33.5337240
6 /30 /1999	105.4449373	6 /30 /2014	30.1191829
12 /30 /1999	103.8064240	12 /30 /2014	26.6977829
6 /30 /2000	102.1201054	6 /30 /2015	23.3710088
12 /30 /2000	100.3787395	12 /30 /2015	20.0000000
6 /30 /2001	98.5873060		

SCHEDULE 3
to
AMENDMENT NO. 1

SPECIAL CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Basic Rent Payment Date -----	Special Casualty Value -----	Basic Rent Payment Date -----	Special Casualty Value -----
6 /30 /1987	104.8372532	12 /30 /2001	95.7032696
and before		6 /30 /2002	93.7144591
12 /30 /1987	103.1747437	12 /30 /2002	91.6578499
6 /30 /1988	104.7074393	6 /30 /2003	89.5387691
12 /30 /1988	106.1105540	12 /30 /2003	87.3479364
6 /30 /1989	107.3878055	6 /30 /2004	85.0911338
12 /30 /1989	108.5567817	12 /30 /2004	82.7585160
6 /30 /1990	109.5987872	6 /30 /2005	80.3563302
12 /30 /1990	110.5177769	12 /30 /2005	77.8741028
6 /30 /1991	111.3137082	6 /30 /2006	75.3186697
12 /30 /1991	111.9864887	12 /30 /2006	72.6788992
6 /30 /1992	112.5305052	6 /30 /2007	69.9622295
12 /30 /1992	112.9537558	12 /30 /2007	67.1568509
6 /30 /1993	113.2388543	6 /30 /2008	64.2708298
12 /30 /1993	113.3835547	12 /30 /2008	61.2916618
6 /30 /1994	113.3689760	6 /30 /2009	58.2281652
12 /30 /1994	113.1911182	12 /30 /2009	55.0670918
6 /30 /1995	112.8293747	6 /30 /2010	51.8180990
12 /30 /1995	112.3984288	12 /30 /2010	48.4671587
6 /30 /1996	111.9493085	6 /30 /2011	45.0248286
12 /30 /1996	111.4812855	12 /30 /2011	41.4763180
6 /30 /1997	110.9936276	6 /30 /2012	37.8331666
12 /30 /1997	109.5081472	12 /30 /2012	34.0798057
6 /30 /1998	107.9574836	6 /30 /2013	30.2651759
12 /30 /1998	106.3540684	12 /30 /2013	26.3015692
6 /30 /1999	104.7547632	6 /30 /2014	22.2767505
12 /30 /1999	103.0580104	12 /30 /2014	18.1935752
6 /30 /2000	101.3085377	6 /30 /2015	14.1491827
12 /30 /2000	99.4986885	12 /30 /2015	10.0000000
6 /30 /2001	97.6329929		

SCHEDULE 4
to
AMENDMENT NO. 1

MODIFIED SPECIAL CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Date	Modified Special Casualty Value	Date	Modified Special Casualty Value
6 /30 /1987	104.7384969	12 /30 /2001	94.6684277
and before		6 /30 /2002	92.5922932
12 /30 /1987	103.0676540	12 /30 /2002	90.4409913
6 /30 /1988	104.5913129	6 /30 /2003	88.2192272
12 /30 /1988	105.9846284	12 /30 /2003	85.9170463
6 /30 /1989	107.2512538	6 /30 /2004	83.5394996
12 /30 /1989	108.4087072	12 /30 /2004	81.0759489
6 /30 /1990	109.4382176	6 /30 /2005	78.5317814
12 /30 /1990	110.3436578	12 /30 /2005	75.8955914
6 /30 /1991	111.1248963	6 /30 /2006	73.1732038
12 /30 /1991	111.7817441	12 /30 /2006	70.3523904
6 /30 /1992	112.3084834	6 /30 /2007	67.4394007
12 /30 /1992	112.7129989	12 /30 /2007	64.4211359
6 /30 /1993	112.9777814	6 /30 /2008	61.3042645
12 /30 /1993	113.1004515	12 /30 /2008	58.0747661
6 /30 /1994	113.0619835	6 /30 /2009	54.7398152
12 /30 /1994	112.8582204	12 /30 /2009	51.2843810
6 /30 /1995	112.4683856	6 /30 /2010	47.7161883
12 /30 /1995	112.0069781	12 /30 /2010	44.0191126
6 /30 /1996	111.5248256	6 /30 /2011	40.2014389
12 /30 /1996	111.0209831	12 /30 /2011	36.2459117
6 /30 /1997	110.4944831	6 /30 /2012	32.1613981
12 /30 /1997	108.9668829	12 /30 /2012	27.9294311
6 /30 /1998	107.3705453	6 /30 /2013	23.5958086
12 /30 /1998	105.7176019	12 /30 /2013	19.0694144
6 /30 /1999	104.0645892	6 /30 /2014	14.4343182
12 /30 /1999	102.3095967	12 /30 /2014	9.6893676
6 /30 /2000	100.4969700	6 /30 /2015	4.9273566
12 /30 /2000	98.6186375	12 /30 /2015	0.0000000
6 /30 /2001	96.6786797		

SCHEDULE 5
to
AMENDMENT NO. 1

EXTRAORDINARY CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Date	Extraordinary Casualty Value	Date	Extraordinary Casualty Value
-----	-----	-----	-----
6 /30 /1987	104.9853877	12 /30 /2001	97.2555323
12 /30 /1987	103.3353784	6 /30 /2002	95.3977078
6 /30 /1988	104.8816290	12 /30 /2002	93.4831378
12 /30 /1988	106.2994424	6 /30 /2003	91.5180820
6 /30 /1989	107.5926331	12 /30 /2003	89.4942714
12 /30 /1989	108.7788934	6 /30 /2004	87.4185851
6 /30 /1990	109.8396415	12 /30 /2004	85.2823668
12 /30 /1990	110.7789555	6 /30 /2005	83.0931534
6 /30 /1991	111.5969262	12 /30 /2005	80.8418699
12 /30 /1991	112.2936057	6 /30 /2006	78.5368686
6 /30 /1992	112.8635379	12 /30 /2006	76.1686623
12 /30 /1992	113.3148911	6 /30 /2007	73.7464726
6 /30 /1993	113.6304636	12 /30 /2007	71.2604233
12 /30 /1993	113.8082096	6 /30 /2008	68.7206778
6 /30 /1994	113.8294649	12 /30 /2008	66.1170054
12 /30 /1994	113.6904650	6 /30 /2009	63.4606903
6 /30 /1995	113.3708582	12 /30 /2009	60.7411579
12 /30 /1995	112.9856049	6 /30 /2010	57.9709651
6 /30 /1996	112.5860328	12 /30 /2010	55.1392278
12 /30 /1996	112.1717391	6 /30 /2011	52.2599131
6 /30 /1997	111.7423444	12 /30 /2011	49.3219273
12 /30 /1997	110.3200437	6 /30 /2012	46.3408193
6 /30 /1998	108.8378911	12 /30 /2012	43.3053675
12 /30 /1998	107.3087681	6 /30 /2013	40.2692269
6 /30 /1999	105.7900243	12 /30 /2013	37.1498013
12 /30 /1999	104.1806308	6 /30 /2014	34.0403991
6 /30 /2000	102.5258893	12 /30 /2014	30.9498867
12 /30 /2000	100.8187650	6 /30 /2015	27.9819218
6 /30 /2001	99.0644626	12 /30 /2015	25.0000000

ARIZONA PUBLIC SERVICE COMPANY

Sale and Leaseback of an Undivided
Interest in Palo Verde Nuclear Generating
Station Unit 2

Security Pacific Capital Leasing Corporation

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PARTICIPATION AGREEMENT

dated as of August 1, 1986

among

SECURITY PACIFIC CAPITAL LEASING CORPORATION,
as Equity Participant

BANK OF AMERICA
NATIONAL TRUST AND SAVINGS ASSOCIATION,
for itself and as Agent for the Original Loan
Participants under the Bank Agency Agreement,
as Agent

PVNGS FUNDING CORP., INC.,
as Funding Corporation

THE FIRST NATIONAL BANK OF BOSTON,
in its individual capacity and as Owner Trustee
under a Trust Agreement,
dated as of August 1, 1986,
with Security Pacific Capital Leasing Corporation, as
Owner Trustee

CHEMICAL BANK
in its individual capacity and as Indenture Trustee
under a Trust Indenture, Mortgage, Security Agreement
and Assignment of Facility Lease, dated as of
August 1, 1986,
with the Owner Trustee, as Indenture Trustee

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest
in Palo Verde Nuclear Generating Station Unit 2
Security Pacific Capital Leasing Corporation

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PARTICIPATION AGREEMENT

THIS PARTICIPATION AGREEMENT, dated as of August 1, 1986, among SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation (the Equity Participant), BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, for itself (Bank of America) and as agent for the Original Loan Participants listed on Schedule 1 hereto (the Agent), PVNGS FUNDING CORP., INC., a Delaware corporation (the Funding Corp), THE FIRST NATIONAL BANK OF BOSTON, a national banking association, in its individual capacity (FNB) and as Owner Trustee (the Owner Trustee) under a Trust Agreement, dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation, CHEMICAL BANK, a New York banking corporation, in its individual capacity (Chemical) and as Indenture Trustee (the Indenture Trustee) under a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, with the Owner Trustee, and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee or APS).

W I T N E S S E T H :

WHEREAS, the Equity Participant desires to cause the Trust to acquire the Undivided Interest and the Real Property Interest and to lease the Undivided Interest and the Real Property Interest to the Lessee under the Facility Lease;

WHEREAS, the Lessee desires to sell the Undivided Interest and the Real Property Interest to the Trust and lease the Undivided Interest and the Real Property Interest back from the Trust under the Facility Lease;

WHEREAS, in order to give effect to the foregoing sale and leaseback, the Owner Trustee and the Lessee are willing to enter into the Purchase Documents with respect to the sale and purchase of the Undivided Interest and the Real Property Interest;

WHEREAS, pursuant to the terms and provisions of the Indenture, the Owner Trustee will authorize the creation, issuance and sale and delivery of the Initial Series Notes and the granting of the security therefor, and the Indenture Trustee will authenticate the Initial Series Notes; and

WHEREAS, the Original Loan Participants are willing to purchase the Initial Series Notes on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For the purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A. References in this Participation Agreement to sections, paragraphs and clauses are to sections, paragraphs and clauses in this Participation Agreement unless otherwise indicated.

SECTION 2. Participation by the Original Loan Participants and Funding Corp; Releveraging; Refunding; Reoptimization.

(a) Original Loan Participants' Commitments; Direction to the Indenture Trustee. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), on the Closing Date each Original Loan Participant agrees to make a secured loan (a Loan) to the Owner Trustee, on a non-recourse basis, in an amount equal to such Original Loan Participant's Loan Percentage of the Facility Cost. The Agent, on behalf of the Original Loan Participants, as purchasers of the Initial Series Notes to be issued on the Closing Date, hereby (i) authorizes and directs the Indenture Trustee to execute, deliver and perform this Participation Agreement and (ii) authorizes and directs the Indenture Trustee to register each Initial Series Note issued on the Closing Date in the names provided to the Indenture Trustee hereunder and, upon authentication and delivery thereof pursuant to this Participation Agreement and the Indenture, to deliver such Initial Series Notes to the Agent. Each Loan Participant acknowledges and agrees, or by becoming a Holder of a Refunding Note will be deemed to have acknowledged and agreed, that, in connection with this Participation Agreement, the Indenture Trustee shall have the benefits and protections of Article VIII of the Indenture and that, in the event of a conflict between the provisions of this Participation Agreement and the Indenture, the Indenture Trustee shall, as between the Indenture Trustee and the Loan

Participants, be fully protected in relying on the express terms of the Indenture.

(b) Failure to Fund. In the event any Original Loan Participant shall fail to make any amount of its Loan available to the Agent pursuant to subsection (c) below, no other Original Loan Participant shall have any obligation to increase any amount of its Loan. In the event the Equity Participant shall fail to make any amount of its Investment available on the Closing Date pursuant to Section 3, the Original Loan Participants shall have no obligation to make any amount of their Loans available on such Date, or to increase any amount of any of their Loans.

(c) Funding of Loans; Fees; Terms of Initial Series Notes.

(i) Not later than the close of business on the Business Day immediately prior to the Closing Date, the Agent shall make available to Chemical funds in an amount equal to the maximum aggregate amount of the Loans specified by Lessee in its Notice of Closing pursuant to Section 5(a), and Chemical shall hold such funds in the Agent's name in a Trust Investment Account (the Investment Account). Chemical shall invest such funds at the direction of the Lessee, with the reasonable consent of the Agent, and earnings on such Investment Account shall be for the account of the Lessee. Subject to the terms and conditions of this Participation Agreement and upon satisfaction of the conditions precedent in Sections 5(a) and 11(a), the Agent shall, on the Closing Date, transfer title to the Investment Account in an amount equal to the actual aggregate amount of the Loans specified by the Lessee in its certificate pursuant to Section 11(a)(2) to the Indenture Trustee for the account of the Owner Trustee.

(ii) On the Closing Date, the Owner Trustee shall pay to the Agent, for the benefit of each Original Loan Participant, a fee equal to one-eighth of one percent ($1/8$ of 1%) of such Original Loan Participant's committed amount set forth on Schedule 1 hereto.

(iii) On the Closing Date, the Lessee shall pay to the Agent an Arrangement Fee as described in that certain letter agreement dated June 27, 1986, between the Lessee and Bank of America.

(iv) The Loans shall be evidenced by one or more Initial Series Notes. The Initial Series Notes shall be issued by the Owner Trustee as registered Notes under and pursuant to the Indenture and shall, in the aggregate, be in the principal amount of the respective Loans, bear interest at the rate or rates per annum and be payable as set forth in the Indenture and the Initial Series Notes.

(d) Request for Refinancing. Subject to Sections 2(e) and 11(c), the Lessee may request by written notice to the Equity Participant, the Loan Participant or Participants, the Owner Trustee and the Indenture Trustee that the Equity Participant arrange for a non-recourse loan (a Refunding Loan) to the Owner Trustee, the proceeds of which shall be used to prepay the aggregate principal amount of Outstanding Notes on the Refunding Date and the expenses incurred in connection therewith. In addition, if any Refunding Loan is to be made following any event referred to in Section 3(d) of the Facility Lease, the Lessee may request, subject to Sections 2(e) and 11(c), that the Equity Participant arrange for an additional simultaneous loan (a Relleveraging Loan) to the Owner Trustee in an amount which shall minimize the Basic Rent payments by the Lessee over the Basic Lease Term while preserving the Equity Participant's Net Economic Return. Subject to the satisfaction of the provisions of this paragraph (d), and further subject to its ability to raise funds, Funding Corp, upon the request of the Lessee, agrees to lend to the Owner Trustee the amount of the applicable Refunding Loan and any simultaneous Relleveraging Loan. In connection with any Refunding Loan, the Lessee may request the Equity Participant to arrange an adjustment to the amounts of principal scheduled to be paid in respect of Outstanding Notes on each Basic Rent Payment Date so as to minimize the Basic Rent payments by the Lessee over the Basic Lease Term while preserving the Equity Participant's Net Economic Return.

(e) Procedures Applicable to and Limitations on Refunding Loans and any Releveraging Loans. Each of the Lessee, the Owner Trustee, the Equity Participant and each Loan Participant agrees that it will cooperate in connection with any Refunding Loan or Releveraging Loan and enter into such additional agreements and such supplements or amendments to or consents under each of the Transaction Documents as may reasonably be requested by the Lessee to effectuate the transactions contemplated in connection with such Refunding Loan and any simultaneous Releveraging Loan; provided, however, that the Lessee may not request more than three Refunding Loans and two Releveraging Loans; and provided, further, that (a) prior to June 30, 1989, the Lessee may request only one Refunding Loan which is not in the form of long-term, fixed-rate non-recourse indebtedness of the Owner Trustee and (b) on and after June 30, 1989, the Lessee may request only one Refunding Loan. Notwithstanding the foregoing, the Equity Participant need not participate in any Refunding Loan or Releveraging Loan or reoptimization (i) which is not in compliance with Revenue Procedure 75-21 and 75-28 (or any similar regulations or procedures), (ii) which would result in the Facility Lease being treated differently for accounting purposes than it was treated immediately prior to such Refunding Loan or Releveraging Loan or reoptimization or (iii) the maturity date of which would extend beyond the scheduled date for the termination of the Basic Lease Term. Proceeds of any Refunding Loan and simultaneous Releveraging Loan shall be paid directly to the Indenture Trustee in immediately available funds at the Indenture Trustee's Office and applied (x) to the extent necessary, to refund the unpaid principal amount of the Outstanding Notes and to pay expenses in connection therewith, and (y) to the extent of the Releveraging Loan, as a partial refund of the Investment. Each Refunding Loan and simultaneous Releveraging Loan shall be aggregated and evidenced by Refunding Notes (the Refunding Notes), in the respective principal amounts requested by the Lessee, each of which Notes shall be issued by the Owner Trustee under and pursuant to the Indenture, be in the respective principal amounts indicated in the foregoing request, bear interest at the respective rates per annum and be payable, in each case as set forth in, or determinable under, the Indenture. The Lessee shall give the parties hereto at least (i) 30 days prior written notice of a proposed Refunding Date and (ii) five Business Days' prior written notice of an actual Refunding Date. Not

less than three Business Days prior to the Refunding Date, the Loan Participant or Participants shall deliver to the Equity Participant and the Lessee a certificate setting forth the information necessary to complete the Refunding Notes (including the respective schedules thereto). Upon such delivery, and upon approval by the Lessee and the Equity Participant of the terms thereof, the Equity Participant and the Lessee shall cause the respective forms of Refunding Notes to be completed. The parties hereto shall cooperate in the preparation and execution of such amendments to the Transaction Documents as shall be necessary or appropriate to effect such refunding; provided, however, that such amendments shall not, in the opinion of independent tax counsel selected by the Equity Participant, adversely affect the tax benefits contemplated by the Equity Participant in entering into the transactions contemplated by this Participation Agreement and the other Transaction Documents.

(f) Reoptimization. Subject to the satisfaction of the conditions set forth in Sections 2(e) and 11(c), if the Lessee, in a timely manner, provides the Owner Trustee and the Equity Participant with information sufficient for the Owner Trustee to direct the adjustments described in Section 3.12 of the Indenture, together with a certificate (in form and substance reasonably satisfactory to the Equity Participant) to the effect that such adjustments minimize the aggregate increase in Basic Rent occurring as a result of the operation of Section 3(d) of the Facility Lease, while preserving Net Economic Return, the Owner Trustee shall deliver to the Indenture Trustee a certificate pursuant to such Section 3.12 of the Indenture. Notwithstanding the foregoing, the Equity Participant and the Owner Trustee may rely on such certificate of the Lessee and shall have no obligation to verify the same.

SECTION 3. Participation by the Equity Participant; Partial Refund of the Investment.

(a) Equity Participant's Commitment. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), on the Closing Date the Equity Participant agrees to provide funds to the Trust as follows: (i) an amount (such amount, as it may be reduced from time to time in accordance with Section 3(b), being herein called the Investment) equal to the Investment Percentage of the Facility Cost for the purpose of

acquiring the Undivided Interest and the Real Property Interest and (ii) an amount equal to Closing Date Transaction Expenses. Proceeds of the Investment shall be made available to the Indenture Trustee, in immediately available funds, at the Indenture Trustee's Office in such manner as the Lessee and the Equity Participant shall agree. Closing Date Transaction Expenses shall be paid to the Owner Trustee, in immediately available funds, at 100 Federal Street, Boston, Massachusetts 02110, Attention: Manager, Corporate Trust Department. In no event shall the sum of the Investment and Transaction Expenses paid by the Owner Trustee pursuant to Section 14 exceed \$30,000,000.

(b) Partial Refund. In the event that the Indenture Trustee shall have received the proceeds of any Releveraging Loan, the Indenture Trustee shall, immediately upon its receipt thereof, disburse the same to the Owner Trustee for disposition in accordance with the Trust Agreement as a partial refund of the Investment, and for purposes hereof the Investment shall thereupon be reduced accordingly.

SECTION 4. Purchase, Sale, Financing and Lease of the Undivided Interest and the Real Property Interest.

(a) The Undivided Interest. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a), receipt from the Equity Participant of the Investment and receipt from the Agent of the proceeds of the Loans made by the Original Loan Participants, the Owner Trustee shall (i) on the Closing Date cause the Trust to purchase the Undivided Interest from the Lessee for the amount specified in the Notice of Closing as the "Purchase Price" (the Purchase Price), and (ii) promptly after receipt of the amount thereof from the Equity Participant, disburse the Closing Date Transaction Expenses, in each case in accordance with the payment instructions in the Notice of Closing. Subject to the satisfaction of the conditions in Section 11(b), on the Closing Date the Lessee shall sell the Undivided Interest to the Trust for the Purchase Price. Concurrently with such purchase and sale, the Trust shall lease the Undivided Interest to the Lessee, and the Lessee shall lease the Undivided Interest from the Trust, pursuant to the Facility Lease.

(b) The Real Property Interest. Subject to the satisfaction of the conditions in Sections 5(a) and 11(a) and receipt from the Equity Participant of the Investment, on the Closing Date the Equity Participant shall cause the Trust to acquire the Real Property Interest from the Lessee for a purchase price equal to the amount set forth in Schedule 2 as the "Real Estate Investment". Subject to the satisfaction of the conditions in Section 11(b), on the Closing Date the Lessee shall sell the Real Property Interest to the Trust for the amount set forth in Schedule 2 as the Real Estate Investment. Concurrently with such purchase and sale, the Trust shall lease the Real Property Interest to the Lessee, and the Lessee shall lease the Real Property Interest from the Trust, pursuant to the Facility Lease.

SECTION 5. Notice of Closing; Closing.

(a) Notice of Closing. Not later than 10:00 a.m., New York time, two Business Days prior to the Closing Date, the Lessee shall deliver to the Equity Participant, the Owner Trustee, the Agent and the Indenture Trustee a notice, substantially in the form of Schedule 2 (the Notice of Closing), which shall (i) state that the Closing Date shall occur on the date specified therein, (ii) list the then known Transaction Expenses payable by the Owner Trustee pursuant to Section 14(a) (the Closing Date Transaction Expenses), (iii) provide payment instructions in respect of the disposition of the Purchase Price, the Real Estate Investment and Closing Date Transaction Expenses and (iv) specify the maximum aggregate amount of the Loans.

(b) Closing. Upon satisfaction or waiver of the conditions in Sections 5(a) and 11(a) and receipt from the Equity Participant of the Investment and the amount of Closing Date Transaction Expenses and from the Agent of the proceeds of the Loans, on the Closing Date the Owner Trustee shall cause the Purchase Price to be paid and the purchase price of the Real Property Interest to be paid and shall disburse Closing Date Transaction Expenses, in each case in funds immediately available on the Closing Date and in accordance with the payment instructions in the Notice of Closing. Upon satisfaction of the conditions in Section 11(b), on or as of the Closing Date the Lessee shall deliver to the Owner Trustee the Purchase Documents.

SECTION 6. Representations, Warranties and Agreements of Funding Corp.

(a) Representations and Warranties. Funding Corp represents and warrants that:

(1) **Due Organization.** Funding Corp is a corporation duly organized and validly existing in good standing under the laws of the State of Delaware and has the corporate power and authority to carry on its business as presently conducted, own its properties, and enter into and perform its obligations under this Participation Agreement.

(2) **Due Authorization.** This Participation Agreement has been duly authorized by all necessary corporate action on the part of Funding Corp and does not require the consent or approval of its stockholder or any trustee or holder of any of its indebtedness or other obligations.

(3) **Execution and Enforceability.** This Participation Agreement has been duly executed and delivered by Funding Corp and constitutes its legal, valid and binding agreement, enforceable against it in accordance with its terms.

(4) **No Violation.** Neither the execution, delivery or performance by Funding Corp of this Participation Agreement, nor the consummation by Funding Corp of the transactions contemplated hereby, nor compliance by Funding Corp with the provisions hereof, conflicts with, or results in the breach of any provision of, or is inconsistent with, the Certificate of Incorporation or By-Laws of Funding Corp or contravenes any Federal, Delaware or New York law applicable to it, or any indenture, mortgage or agreement to which Funding Corp is a party or by which it or its property is bound, or requires any Governmental Action with respect to Funding Corp on or before the Closing Date under any Federal, Delaware or New York law applicable to it.

(5) **No Other Business.** Except as contemplated by this Participation Agreement, the other Transaction Documents and any Financing Documents and except as otherwise contemplated by the Section 6(c) Application, Funding Corp has not

engaged in any business or activity of any type or kind whatever.

(6) ERISA. Funding Corp will not acquire any Refunding Note with the "plan assets" of any "employee benefit plan", within the meaning of Section 3(3) of ERISA, or any "plan", within the meaning of Section 4975(e)(1) of the Code.

(7) Investment Representation. Funding Corp will acquire each Refunding Note to be acquired by it hereunder and under the Indenture solely for purposes of pledging such Refunding Note to the Collateral Trust Trustee to secure Bonds issued from time to time under the Collateral Trust Indenture. Funding Corp understands that no Refunding Note to be acquired by it hereunder or under the Indenture will have been registered under the Securities Act and that each such Refunding Note will bear the legend set forth in Section 4.5 of the Indenture.

(b) Agreements. Funding Corp agrees that:

(1) Transfers of Notes. Any transfer or assignment of any Note acquired by it or of all or any part of Funding Corp's interest hereunder or under any other Transaction Document or any Financing Document shall be effected in a transaction constituting an exempted transaction under the Securities Act and on the express condition that the transferee, assignee or participant shall agree to be bound by the terms and provisions hereof and thereof. Neither Funding Corp nor any subsequent Holder of a Note may sell, exchange or transfer any Note to any other Person (other than the Collateral Trust Trustee) unless such transferee delivers to the Lessee, the Equity Participant, the Owner Trustee and the Indenture Trustee a representation and warranty (and an opinion of counsel satisfactory to each such Person) to the effect that neither the transfer of such Note to, nor the ownership of such Note by, such transferee will cause such transferee, or any such Persons, to be engaged in a "prohibited transaction", as defined in section 406 of ERISA or section 4975 of the Code, which is not at such time subject to an exemption contained in ERISA or in the rules, regulations, releases or bulletins adopted thereunder.

(2) Prepayment of Bonds. Except as provided in this Participation Agreement, Funding Corp will not refinance or optionally prepay any Bond issued in connection with any Refunding Note without the consent of the Equity Participant and the Lessee.

(3) Quiet Enjoyment. Funding Corp acknowledges Section 6(a) of the Facility Lease.

(4) No Other Business. During such time as any Note acquired by Funding Corp is outstanding and held by the Collateral Trust Trustee as security for obligations of Funding Corp, Funding Corp will not (i) engage in any business or activity other than (1) in connection with the Transaction Documents or (2) as otherwise contemplated by the Section 6(c) Application or (ii) amend or engage in any activity or take any action not permitted by Article THIRD, FOURTH or SIXTH of its Certificate of Incorporation, as in effect on the date of execution and delivery hereof, without, in each case, the consent of the Lessee, the Equity Participant, the Owner Trustee and the Indenture Trustee.

(c) Agreements With the Indenture Trustee. Funding Corp hereby (i) acknowledges and agrees that, in connection with this Participation Agreement, the Indenture Trustee shall have the benefits and protections of Article VIII of the Indenture and (ii) agrees that, to the extent it becomes a Loan Participant, in the event of a conflict between the provisions of this Participation Agreement and the Indenture, the Indenture Trustee shall, as between the Indenture Trustee and Funding Corp, be fully protected in relying on the express terms of the Indenture.

SECTION 7. Representations, Warranties and Agreements of the Equity Participant.

(a) Representations and Warranties. The Equity Participant represents and warrants that:

(1) Due Organization. The Equity Participant is a corporation duly organized and validly existing in good standing under the laws of the State of Delaware and has the corporate power and authority to enter into and perform its obligations under this Participation Agreement and each other Transaction Document to which it is a party.

(2) Due Authorization. This Participation Agreement and each other Transaction Document to which the Equity Participant is a party have been duly authorized by all necessary corporate action on the part of the Equity Participant and do not require the consent or approval of its stockholder or any trustee or holder of any of its indebtedness or other obligations, except such as have been duly obtained, given or accomplished.

(3) Execution and Enforceability. This Participation Agreement and each other Transaction Document to which the Equity Participant is a party have been duly executed and delivered by the Equity Participant and constitute its legal, valid and binding agreement, enforceable against it in accordance with its terms.

(4) No Violation. Neither the execution, delivery or performance by the Equity Participant of this Participation Agreement or any other Transaction Document to which it is a party, nor the consummation by the Equity Participant of the transactions contemplated hereby or thereby, nor compliance by the Equity Participant with the provisions hereof or thereof, conflicts with, or results in the breach of any provision of, or is inconsistent with, its documents of incorporation or By-Laws or contravenes any Applicable Law applicable to it, or any indenture, mortgage or agreement for borrowed money to which the Equity Participant is a party or any other agreement or instrument to which the Equity Participant is a party or by which it or its property is bound or requires any Governmental Action with respect to the Equity Participant under Federal, New York, Delaware or California law applicable on or before the Closing Date, except such as are contemplated by the Transaction Documents or such as have been duly obtained, given or accomplished; provided, however, that the Equity Participant makes no representation or warranty as to any Applicable Law or Governmental Action relating to the Securities Act (other than as expressly set forth in clause (8) of this Section 7(a)), the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear

matters, public utilities, the environment, health and safety or Unit 2.

(5) No Equity Participant's Liens. Neither the execution and delivery by the Equity Participant of this Participation Agreement or any other Transaction Document to which the Equity Participant is, or is to become, a party, nor the performance by the Equity Participant of its obligations hereunder or thereunder, will subject the Trust Estate or the Lease Indenture Estate, or any portion of either thereof, to any Equity Participant's Lien.

(6) Acquisition for Investment. The Equity Participant is acquiring the beneficial interest in the Trust and the Trust Estate for its own account, for investment and not with a view to, or for sale in connection with, any distribution thereof in violation of Section 5 of the Securities Act; provided, however, that nothing herein shall prohibit a disposition of the Equity Participant's property in compliance with all Applicable Law.

(7) No Prior Security Interest. There exists no security interest in or other Lien on the Lease Indenture Estate in the States of Arizona, Delaware or California arising as a result of claims against the Equity Participant unrelated to the transactions contemplated by the Transaction Documents which is prior to the Indenture Trustee's security interest in and Lien on the Lease Indenture Estate.

(8) Securities Act. The Equity Participant has not directly or indirectly offered or sold, or authorized anyone to directly or indirectly offer or sell, any security issued or to be issued to finance Unit 2, or any security the offering of which for the purposes of the Securities Act would be deemed to be part of the offerings contemplated by the Transaction Documents, or solicited any offer to acquire any such security from any Person, in violation of Section 5 of the Securities Act.

(9) ERISA. The Equity Participant is not acquiring its interest in the Trust with the "plan assets" of any "employee benefit plan" within the meaning of section 3(3) of ERISA or any "plan" within the meaning of section 4975(e)(1) of the Code.

(10) Location of the Chief Executive Office. The chief executive office of the Equity Participant for purposes of Article 9 of the UCC is at Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV.

(b) Agreements. The Equity Participant agrees and, to the extent set forth in Section 7(b)(4), the Lessee also agrees that:

(1) No Equity Participant's Liens. The Equity Participant will not create or permit to exist, and, at its own cost and expense, will promptly take such action as may be necessary duly to discharge, all Equity Participant's Liens.

(2) Quiet Enjoyment. The Equity Participant acknowledges the provisions of Section 6(a) of the Facility Lease and Section 8(c) of this Participation Agreement.

(3) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, the Equity Participant will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of, or in respect of, Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(4) Transfer of Interest in the Trust Estate. If the Lessee shall not have assumed the Notes as contemplated by Section 3.9(b) of the Indenture and the Lessor shall not have Transferred the Undivided Interest to the Lessee in accordance with Section 9(c), 9(d) or 16(e) of the Facility Lease, then, upon receipt by the Equity Participant, from the Indenture Trustee or otherwise, of the payments specified in Sections 9(c), 9(d) or 16(e) of the Facility Lease, the Equity Participant shall assign, convey and transfer (the Special Transfer) to the Lessee all of the Equity Participant's right, title and interest in, to and under the Trust Estate (except Excepted Rights and the right to receive Excepted Payments), such transfer to be effected by the execution and delivery by the Equity Participant

of a Bill of Sale and Assignment substantially in the form of Appendix B hereto but without any further act (whether under any Transaction Document or otherwise) by the Owner Trustee, the Equity Participant, any Loan Participant, the Lessee, the Indenture Trustee or any other Person, whereupon the Lessee shall be deemed for all purposes to have assumed, and the Equity Participant shall be deemed for all purposes to have been released from, all obligations and liabilities of the Equity Participant under this Participation Agreement and the other Transaction Documents (other than in respect of obligations under Sections 7(b)(1), (2) and (3) of this Participation Agreement incurred prior to the effectuation of the Special Transfer which shall survive, and shall continue in effect following, the Special Transfer). At any time following the occurrence of an Event of Loss or a Deemed Loss Event, or at any time when an Event of Default shall have occurred and be continuing, the Equity Participant may effect the Special Transfer, whether or not the Equity Participant shall have received the payments referred to in the preceding sentence or the payments specified in Section 16(a) of the Facility Lease, as the case may be, whereupon (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding, and (ii) the Facility Lease shall become a security agreement for all purposes of Applicable Law.

If at the time of the Special Transfer the Equity Participant shall not have received the payments specified in the first sentence of the preceding paragraph or the payments specified in Section 16(a) of the Facility Lease, as the case may be, the obligation of the Lessee to make such payments (together with interest thereon at the Penalty Rate) shall continue until so received, and such obligation shall be secured by (and the Lessee hereby grants to the Equity Participant a security interest in and general lien upon) all the Lessee's right, title and interest in, to and under the Trust Estate. In connection therewith, the Lessee hereby agrees that (i) the Equity Participant shall have all the rights and remedies of a secured party under

the UCC, (ii) the Lessee hereby appoints the Equity Participant as its attorney-in-fact, irrevocably, with full power of substitution, to ask, require, demand, receive and give acquittance for any and all moneys and claims for moneys due and to become due to the Lessee under or arising out of the Trust Estate, to endorse any checks or other instruments or orders in connection therewith, and to take any action (including the filing of financing statements or other documents and the delivery of written instructions to the Owner Trustee and the Indenture Trustee specifying that all payments to be made to the Lessee under the Trust Agreement and the Indenture shall be made directly to the Equity Participant) or institute any proceedings which the Equity Participant may deem necessary or appropriate to protect and preserve such security interest and the rights of the Equity Participant to receive payments thereunder, (iii) until all amounts due to the Equity Participant have been received by the Equity Participant, the Lessee (in its capacity as such and as transferee under the Special Transfer) shall not, without the prior written consent of the Equity Participant, take any action or deliver any instruction under, or accept or approve any amendment to, any Transaction Document the effect of which would be to (A) relieve or otherwise affect the obligation of the Lessee to make such payments, (B) terminate the Trust Agreement, (C) terminate or rescind the Facility Lease or (D) sell, assign, transfer or deliver the Trust Estate to any Person and (iv) the Lessee agrees, from time to time, to do all such acts and execute all such instruments of further assurance as shall be reasonably requested from time to time by the Equity Participant for the purpose of fully carrying out and effectuating this Section 7(b)(4) and the intent hereof.

On the date which is 100 days after the receipt by the Equity Participant of all amounts due to the Equity Participant, the security interest and lien hereinabove provided shall, so long as the Lessee is not then the subject of any bankruptcy, insolvency or similar proceeding, terminate, and the Equity Participant, at the request of the Lessee, shall execute and deliver to the Lessee such termination statements, releases or other instruments presented to the Equity Participant as shall be reasonably required to effect such termination.

Following an Event of Loss, a Deemed Loss Event or the exercise of the Cure Option, the Lessee shall promptly commence and diligently pursue best efforts to (i) satisfy all of the conditions set forth in Section 3.9(b) of the Indenture and (ii) assume the obligations represented by the Initial Series Notes, notwithstanding any intervening Special Transfer.

The Lessee warrants to and for the benefit of the Holders of Notes that a Special Transfer effected in accordance with the provisions of this Section 7(b)(4) will not invalidate, impair, interrupt or otherwise restrict the Lessee's obligation to pay Rent in accordance with the terms of the Facility Lease or the Lessor's rights and remedies with respect to such obligation. The Lessee covenants that it will designate an Affiliate as transferee in connection with a Special Transfer if such designation is necessary to prevent a breach of the warranty in the foregoing sentence. The Lessee agrees that (i) it will provide to the Indenture Trustee an opinion of counsel, in form and substance satisfactory to the Indenture Trustee, to the effect that the Special Transfer did not, at the time thereof (or, if delivered prior to the Special Transfer, will not), invalidate, impair, interrupt or otherwise restrict the Lessee's obligation to pay Rent in accordance with the terms of the Facility Lease, (ii) the opinion of counsel described in subclause (i) of this sentence will, if practicable in the Lessee's judgment, be delivered to the Indenture Trustee prior to the Special Transfer, but in no event before the date on which the event giving rise to the Special Transfer occurred or more than 30 days after the date of the Special Transfer, and (iii) if the opinion of counsel described in subclause (i) of this sentence is not delivered in accordance with subclause (ii) of this sentence, such non-delivery shall be deemed to be and shall conclusively establish that the Lessee breached the warranty contained in the first sentence of this paragraph. Anything to the contrary notwithstanding, nothing herein shall be construed or interpreted to mean or imply that the Equity Participant or the Lessee cannot effect a Special Transfer on the terms and in the manner described herein or that a breach of the Lessee's warranty in the first sentence of this paragraph shall affect in any way

the Equity Participant's entitlement to payment in accordance with this Section 7(b)(4).

SECTION 8. Representations, Warranties and Agreements of the Owner Trustee and FNB.

(a) Representations and Warranties. FNB as Owner Trustee and (except as otherwise provided in the last sentence of this Section 8(a)) in its individual capacity, represents and warrants that:

(1) Due Organization. FNB is a national banking association duly organized and validly existing in good standing under the laws of the United States of America and has all requisite corporate power and authority to enter into and perform its obligations under (x) the Trust Agreement and, to the extent it is a party hereto in its individual capacity, this Participation Agreement and (y) acting as Owner Trustee, this Participation Agreement and each other Transaction Document to which FNB is a party as Owner Trustee.

(2) Due Authorization; Enforceability; etc. This Participation Agreement and each other Transaction Document to which FNB is a party have been duly authorized by all necessary corporate action of FNB (in its individual capacity or as Owner Trustee, as the case may be) and, upon execution and delivery hereof and thereof, this Participation Agreement and each such other Transaction Document will have been duly executed and delivered and will be a legal, valid and binding agreement of FNB (in its respective capacities), enforceable against it (in its respective capacities) in accordance with its terms; it being understood that FNB is not making any representation or warranty as to the priorities of the Liens created or to be created under any Transaction Document, title to the Trust Estate or recordings or filings necessary in connection therewith.

(3) Notes. Upon execution of each Note to be issued by the Owner Trustee under the Indenture pursuant hereto, authentication thereof by the Indenture Trustee pursuant to the Indenture and delivery thereof against payment therefor in accordance with this Participation Agreement, such Note will be a legal, valid and binding obligation

of the Owner Trustee, enforceable against the Owner Trustee in accordance with its terms.

(4) No Violation. Neither the execution and delivery by (x) FNB of the Trust Agreement and, to the extent FNB is a party hereto in its individual capacity, this Participation Agreement and (y) the Owner Trustee of this Participation Agreement and each other Transaction Document (other than the Trust Agreement) to which the Owner Trustee is a party, nor the performance by FNB, in its individual capacity or as Owner Trustee, as the case may be, of its obligations under each thereof, conflicts with, or results in the breach of any provision of, its Articles of Association or By-Laws and does not contravene any Applicable Law of the United States of America or The Commonwealth of Massachusetts governing the banking or trust powers of FNB, and does not contravene any provision of, or constitute a default under, any indenture, mortgage, contract or other instrument to which FNB is a party or by which it is bound or require any Governmental Action with respect to the Owner Trustee under any Federal or Massachusetts law, except such as are contemplated by the Transaction Documents or such as have been duly obtained, given or accomplished; provided, however, that no representation or warranty is made with respect to (i) the right, power or authority of FNB or the Owner Trustee to act under the ANPP Participation Agreement or the License in respect of the Undivided Interest or Unit 2, (ii) as to any Applicable Law or Governmental Action relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Nuclear Waste Act, the Federal Power Act, the Atomic Energy Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 or (iii) the Trust Estate or the Lease Indenture Estate to the extent either may constitute real property under Applicable Law.

(5) Defaults. To the best knowledge of the Owner Trustee, no Indenture Default or Indenture Event of Default has occurred and is continuing. The Owner Trustee is not in violation of any of the terms of this Participation Agreement or any other Transaction Document to which it is a party.

(6) Litigation. There is no action, suit, investigation or proceeding pending or, to the knowledge of FNB, threatened against FNB (in any capacity) before any court, arbitrator or administrative or governmental body and which relates to its banking or trust powers which, individually or in the aggregate, if decided adversely to the interests of FNB in such capacity, would have an adverse effect upon the ability of FNB (in any capacity) to perform its obligations under this Participation Agreement or any other Transaction Document to which it (in any capacity) is a party.

(7) Location of the Chief Place of Business and Chief Executive Office, etc. The chief place of business and chief executive office of the Owner Trustee and the office where its records concerning the accounts or contract rights relating to the transactions contemplated hereby are kept are located in Boston, Massachusetts.

(8) No Prior Security Interest. There exists no security interest in the Lease Indenture Estate in the State of New York or Arizona or in The Commonwealth of Massachusetts arising as a result of any claim against FNB unrelated to the transactions contemplated by the Transaction Documents or the Financing Documents which is prior to the Indenture Trustee's security interest in the Lease Indenture Estate.

(9) No Lessor's Liens. Neither the execution by FNB (in any capacity) of this Participation Agreement or any other Transaction Document to which it (in any capacity) is a party, nor the performance in such capacity by it of its obligations hereunder or thereunder, will subject the Trust Estate or the Lease Indenture Estate, or any portion thereof, to any Lessor's Lien.

The representations and warranties in Section 8(a)(2) and Section 8(a)(3), as to Transaction Documents and each Note being legal, valid and binding obligations enforceable in accordance with their respective terms, are given only by FNB in its capacity as Owner Trustee and not in its individual capacity, except that FNB does represent in its individual capacity that it is authorized under the laws of The Commonwealth of

Massachusetts to execute and deliver the Transaction Documents to which it is a party.

(b) Agreements. FNB agrees, in its individual capacity, that:

(1) Discharge of Liens. FNB will not create or permit to exist, and will, at its own cost and expense, promptly take such action as may be necessary duly to discharge, all Lessor's Liens.

(2) Certain Amendments. Unless a Default or an Event of Default has occurred and is continuing or an Event of Loss or Deemed Loss Event has occurred, FNB will not amend any of the payment terms of any Note or take any action to refund any Note after the date of issue thereof pursuant to the terms of this Participation Agreement and the Indenture without the prior written consent of the Lessee. Except for amendments or supplements made pursuant to Article X of the Trust Agreement or contemplated by Section 7(b)(4), FNB will not amend or supplement, or consent to any amendment of or supplement to, the Trust Agreement without the prior written consent of the Lessee unless a Default or an Event of Default has occurred and is continuing or the Lease Termination Date has occurred or an Event of Loss or Deemed Loss Event has occurred, if such amendment would materially and adversely affect the rights of the Lessee under the Facility Lease or this Participation Agreement.

(3) Change in Location of Chief Place of Business and Chief Executive Office, etc. FNB shall notify the Lessee, the Loan Participant, the Equity Participant, Funding Corp and the Indenture Trustee promptly after any change in the location of its chief executive office, principal and chief place of business or place where its records concerning the accounts or contract rights relating to the transactions contemplated hereby are kept.

(4) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, FNB (in any capacity) agrees that it will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in

respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(5) Quiet Enjoyment. FNB acknowledges Section 6(a) of the Facility Lease.

(c) Agreements. The Owner Trustee agrees that:

(1) Rights in Relation to ANPP Participants. The rights and remedies of the Owner Trustee and the Equity Participant in the Undivided Interest and in the Real Property Interest are subject and subordinate to the rights and remedies of the ANPP Participants (other than (i) the Lessee or (ii) any Person who shall become an ANPP Participant in respect of the Lessor's Interest) under the ANPP Project Agreements.

(2) Lessee to be an ANPP Participant. Except as provided in Sections 15.2.2, 15.6.4 and 15.10 (or any comparable successor provisions) of the ANPP Participation Agreement, the Lessee shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Lessor and the Indenture Trustee) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of the Lessee transferred to the Lessor pursuant to the Transaction Documents; provided, however, that the foregoing shall not limit in any way any liability or obligation that the Lessee may incur to the Owner Trustee or the Equity Participant under any Transaction Document as a result thereof.

(3) Cash Bids. On the Lease Termination Date and upon the Lessee failing to purchase or otherwise reacquire all the right, title and interest in PVNGS and contractual rights related thereto necessary for the operation of the interest (the Lessor's Interest) acquired by the Lessor pursuant to the Transaction Documents, the Lessor shall, and, subject to the rights of the Lessee to renew for the Renewal Term or purchase the Undivided Interest and the Real Property Interest pursuant to the Facility Lease, at any time prior to the Lease Termination

Date the Lessor may, entertain cash bids from each ANPP Participant for the Lessor's Interest.

(4) Survival. The provisions of Sections 8(c)(1), (2) and (3) shall remain in full force and effect until such time as the ANPP Administrative Committee or the ANPP Participants shall otherwise consent, by amendment to the ANPP Participation Agreement or otherwise.

(5) License Matters. The Owner Trustee acknowledges that before taking possession of the Undivided Interest or the Real Property Interest or any part thereof or of any other interest in PVNGS, either of the following may be required: (i) the issuance of an appropriate license from the NRC, whether by amendment to the License or otherwise, or (ii) a partial transfer of the License authorizing the Lessor to possess its interest in PVNGS, to the extent of the Undivided Interest, upon application for partial transfer of the License to such extent filed pursuant to Applicable Law.

SECTION 9. Representations, Warranties and Agreements of Chemical.

(a) Representations and Warranties. Chemical represents and warrants that:

(1) Due Organization. Chemical is a banking corporation duly organized and validly existing in good standing under the laws of the State of New York and has the corporate power and authority and legal right to enter into and perform its obligations under the Indenture, this Participation Agreement and each other Transaction Document to which it is a party.

(2) Due Authorization; Enforceability, etc. This Participation Agreement and each other Transaction Document to which Chemical is a party have been duly authorized by all necessary corporate action on the part of Chemical and each has been duly executed and delivered by Chemical.

(3) Authentication of Each Note. The officer of Chemical who shall authenticate any Note to be issued pursuant to the Indenture shall be, at the time of such authentication, an Authorized Officer.

(4) No Violation. Neither the execution and delivery by Chemical of this Participation Agreement or the Indenture, nor the authentication by it of the Notes, nor the consummation by it of the transactions contemplated hereby or thereby, nor the compliance by it with the provisions hereof or thereof will contravene any Applicable Law governing its banking or trust powers, or contravene or result in a breach of, or constitute a default under, its Articles of Incorporation or By-laws, or require any Governmental Action under any Federal or New York or Arizona law, except such as have been, or on or before the Closing Date will have been, duly obtained, given or accomplished; provided, however, that no representation or warranty is made as to (i) any Applicable Law or Governmental Action relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Nuclear Waste Act, the Federal Power Act, the Atomic Energy Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 or (ii) the Lease Indenture Estate to the extent it may constitute real property under Applicable Law.

(b) Agreements. The Indenture Trustee agrees that:

(1) Agreement to Discharge Liens. The Indenture Trustee will not create or permit to exist, and will promptly take such action as may be necessary duly to discharge, all Indenture Trustee's Liens.

(2) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of the Collateral Trust Indenture, the Indenture Trustee agrees that it will not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(3) Quiet Enjoyment. The Indenture Trustee acknowledges Section 6(a) of the Facility Lease.

SECTION 10. Representations, Warranties and Agreements of the Lessee.

(a) Representations and Warranties. The Lessee represents and warrants that:

(1) Due Organization. APS is a corporation duly organized and validly existing in good standing under the laws of the State of Arizona and has the corporate power and authority to carry on its business as presently conducted, to own or hold under lease its properties and to enter into and perform its obligations under this Participation Agreement and each other Transaction Document to which it is a party. APS is duly qualified and in good standing to do business as a foreign corporation in the State of New Mexico and has not failed to qualify to do business or to be in good standing in any other jurisdiction where failure so to qualify or be in good standing would materially and adversely affect the financial condition of APS or its ability to perform any obligations under this Participation Agreement or any other Transaction Document to which it is a party. All of the issued and outstanding common stock of APS is owned by AZP Group, Inc.

(2) Due Authorization. The execution, delivery and performance by APS of this Participation Agreement and each other Transaction Document to which it is a party have been duly authorized by all necessary corporate action on the part of APS and do not, and will not, require the consent or approval of AZP Group, Inc. or any trustee or holder of any indebtedness or other obligation of APS, other than (i) the Mortgage Release, (ii) the finding of the ANPP Administrative Committee described in Section 15.6.2 of the ANPP Participation Agreement and (iii) such other consents and approvals as have been, or on or before the Closing Date, in the case of the Transaction Documents, or on or before any Refunding Date, in the case of any Refunding Loan, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant.

(3) Execution. This Participation Agreement and each other Transaction Document to which the Lessee is a party have been duly executed and delivered by APS, and this Participation Agreement

and each such Transaction Document constitute the legal, valid and binding agreements of APS, enforceable against it in accordance with their respective terms.

(4) No Violation, etc. Neither the execution, delivery or performance by the Lessee of this Participation Agreement or any other Transaction Document to which it is a party, nor the consummation by the Lessee of the transactions contemplated hereby or thereby, nor compliance by the Lessee with the provisions hereof or thereof, conflicts or will conflict with, or results or will result in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or By-Laws of APS or any Affiliate of APS, or any Applicable Law, or any indenture, mortgage, lease or any other agreement or instrument to which APS or any Affiliate of APS is a party or by which the property of APS or any Affiliate of APS is bound, or results or will result in the creation or imposition of any Lien (other than Permitted Liens) upon any property of APS or any Affiliate of APS. There is no provision of the Restated Articles of Incorporation or By-Laws of APS, or any Applicable Law, or any such indenture, mortgage, lease or other agreement or instrument which materially adversely affects, or in the future is likely (so far as the Lessee can now foresee) to materially adversely affect, the business, operations, affairs, condition, properties or assets of the Lessee, or its ability to perform its obligations under this Participation Agreement or any other Transaction Document to which it is a party.

(5) Governmental Actions. No Governmental Action under any Federal (including, without limitation, the Federal Power Act), Arizona or New York law is or will be required in connection with the execution, delivery or performance by the Lessee of, or the consummation by the Lessee of the transactions contemplated by, this Participation Agreement or any other Transaction Document to which it is a party, except such Governmental Actions (i) as have been, or on or before the Closing Date, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant, (ii) as may be required under existing Federal, Arizona or New York

law to be obtained, given or accomplished from time to time after the Closing Date in connection with the maintenance, use, possession or operation of Unit 2 or otherwise with respect to Unit 2 and the Lessee's or the Operating Agent's involvement therewith and which are, for PVNGS, routine in nature and which the Lessee has no reason to believe will not be timely obtained, (iii) as may be required under Applicable Law not now in effect and (iv) as may be required in connection with any Refunding Loan (which will have been duly obtained, given or accomplished by the Refunding Date). No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required (a) in connection with the participation by the Owner Trustee, the Indenture Trustee, Funding Corp, the Equity Participant, or any Loan Participant in the consummation of the transactions contemplated by this Participation Agreement, any other Transaction Document or any Financing Document or (b) to be obtained by any of such Persons during the Lease Term, except such Governmental Actions (i) as have been, or on or before the Closing Date, in the case of the Transaction Documents, or any Refunding Date, in the case of any Refunding Loan or any Financing Documents, will have been, duly obtained, given or accomplished, with true copies thereof delivered to the Equity Participant and the Loan Participant, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of any obligations issued under and pursuant to the Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required by existing Applicable Law if, after the Lease Termination Date,

the Lessee should redeliver the Undivided Interest to the Lessor pursuant to Section 5(a) of the Facility Lease or provide transmission services for the Owner Trustee and sell an undivided interest in the Retained Assets to the Lessor as provided under the Assignment and Assumption, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person in connection with taking possession of its interest in Unit 2. Nothing in the License or the License Amendment or any other Governmental Action with respect to the NRC will materially interfere with the ability of the Owner Trustee to transfer or convey the Undivided Interest and the Real Property Interest to a person, partnership, corporation or governmental corporation or agency engaged in the generation, transmission or distribution of energy who will be in a position to enjoy all the benefits of, have all the rights of, and be an ANPP Participant, so long as such person, partnership, corporation or governmental corporation or agency complies with the licensing requirements of the NRC and obtains; or becomes a transferee of, a license from the NRC.

(6) Securities Act. Neither APS nor anyone acting on its behalf has directly or indirectly offered or sold any Bond, any interest in any Note, any note issued with respect to any other undivided interest in Unit 2, the Undivided Interest or any other undivided interest in Unit 2, the Facility Lease or any other lease of an undivided interest in Unit 2, or any similar security or lease, or any interest in any security or lease the offering of which, for purposes of the Securities Act, would be deemed to be part of the same offering as the offering of the aforementioned securities or leases, or solicited any offer to acquire any of the aforementioned securities or leases, in each case in a manner which would constitute a violation of Section 5 of the Securities Act, and except as contemplated by this Participation Agreement, neither the Lessee nor any one authorized to act on its behalf will take any action which would subject the issuance or sale of any Note or any interest in the Facility Lease or any other debt instrument (other than the Bonds) issued or to be issued to finance the Undivided Interest to the registration requirements of such Section 5.

(7) Title to the Undivided Interest; Real Property Interest; Security Interest. On the Closing Date, (i) good and marketable title to the Undivided Interest will be duly, validly and effectively conveyed and transferred to the Owner Trustee, free and clear of all Liens other than the Liens indicated on the title report delivered pursuant to Section 11(a)(30) and other Liens relating to obligations not in excess of \$15,000,000, (ii) good and marketable title to the Real Property Interest will be duly, validly and effectively created in the Owner Trustee, as provided in the Deed, (iii) APS will have good and marketable title to its ownership interest in the Retained Assets, free and clear of all Liens except Permitted Liens, the lien of the Existing Mortgage and matters disclosed in the title report referred to in Section 11(a)(30), (iv) the Lessee will have good and valid title to its ownership interest in the PVNGS Site, (v) Unit 2 will be wholly located on the PVNGS Site without any material encroachments by any portion thereof on any other property, (vi) all filings and recordings necessary or advisable to perfect the Owner Trustee's right, title and interest in and to the Undivided Interest and the Real Property Interest, and to perfect for the benefit of the Indenture Trustee and the holders of the Notes, the security interest, mortgage and assignment of facility lease provided for in the Indenture, will in each case have been duly made and (vii) no other action, including any action under any fraudulent conveyance statute, will be required to protect the title and interests of the Owner Trustee in and to the Undivided Interest and Real Property Interest, in each case against the claims of all Persons other than the ANPP Participants under the ANPP Project Agreements, or to perfect such security interest, mortgage and assignment of facility lease in favor of the Indenture Trustee.

(8) Non-Interference. None of the Permitted Liens described in clauses (ii), (iii), (iv), (v), (vii), (viii) and (xii) of the definition of such term will, on and after the Closing Date, materially interfere with the use or possession of the Undivided Interest or the Real Property Interest or the use of or the exercise by the Owner Trustee of its rights under the Purchase Documents and the Assignment and Assumption with respect to the

interests in PVNGS granted or to be granted under the Purchase Documents and the Assignment and Assumption. Nothing in the ANPP Participation Agreement or in any ANPP Project Agreement will materially interfere with the ability of the Owner Trustee to transfer or convey the Undivided Interest and the Real Property Interest to a person, partnership, corporation or governmental corporation or agency engaged in the generation, transmission or distribution of energy, who will be in a position to enjoy all the benefits of, have all the rights of, and be an ANPP Participant.

(9) Personal Property. Unit 2, based on the agreements of the Lessee and the other ANPP Participants in the ANPP Participation Agreement and of the Lessee and the Owner Trustee herein and in the other Transaction Documents, is to the full extent permitted by Applicable Law personal property.

(10) Location of Chief Executive Office. The chief executive office and place of business of the Lessee and the office where it keeps its records concerning its accounts or contract rights is located at 411 North Central Avenue, Phoenix, Arizona 85004.

(11) Financial Statements. The consolidated balance sheets of APS (A) as of December 31, 1985 and 1984, respectively, and the related consolidated statements of income, retained earnings and changes in financial position for each of the years in the three-year period ended December 31, 1985, together with the notes accompanying such financial statements, all certified by Deloitte Haskins & Sells, and (B) as of June 30, 1986 and 1985, respectively, and the related consolidated statements of income, retained earnings and changes in financial position for the six-month periods ended June 30, 1986 and June 30, 1985, respectively, all certified by the Treasurer or an Assistant Treasurer of APS, as furnished to the Equity Participant and the Original Loan Participants, fairly present the consolidated financial position of APS at each such date and the results of its operations for each of the periods then ended, in conformity with generally accepted accounting principles applied on a consistent basis, subject in the case of the consolidated balance

sheets and the related consolidated statements described in clause (B) above, to the condensation of certain financial information and the omission of certain footnote disclosures as permitted by the rules and regulations of the SEC and to year-end audit adjustments. The Lessee knows of no such adjustments which would, if made on the date hereof, be material.

(12) Disclosure. None of the financial statements to which reference is made in paragraph 11 above, nor the reports to which reference is made in this paragraph 12, nor any certificate, written statement or other document prepared by or for, or at the direction of, the Lessee and furnished to the Equity Participant by the Lessee in connection with the transactions contemplated hereby (under the circumstances, at the time and for the purposes for which any statement made therein was made) contains any untrue statement of a material fact or omits to state a material fact necessary to make the statements therein not misleading. There is no fact known to the Lessee that materially and adversely affects or, so far as the Lessee can now reasonably foresee, is likely to materially and adversely affect, the business or financial condition of APS or any material portion of its properties or the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document or Financing Document to which the Lessee is, or is to become, a party except as disclosed in APS's Annual Report on Form 10-K for the year ended December 31, 1985, APS's Quarterly Reports on Form 10-Q for the quarters ended March 31, 1986 and June 30, 1986, respectively, and APS's Current Reports on Form 8-K filed on January 22, 1986 and June 19, 1986, copies of which have been provided to the Equity Participant.

(13) Litigation. There is no action, suit, investigation or proceeding pending or, to the knowledge of the Lessee, threatened against APS before any court, arbitrator or administrative or governmental body which questions the validity or enforceability of this Participation Agreement or any other Transaction Document and, except as disclosed in the reports to which reference is made in paragraph 12, there is no action, suit, investigation or proceeding pending or, to the best

knowledge of the Lessee, threatened against APS before any court, arbitrator or administrative or governmental body which, individually or in the aggregate, if decided adversely to the interests of the Lessee, would have a material adverse effect on the business or financial condition of APS or materially and adversely affect the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document or Financing Document to which it is, or is to become, a party.

(14) Tax Returns. The Lessee has filed all Federal, state, local and foreign, if any, tax returns which were required to be filed, and has paid all Taxes shown to be due and payable on such returns and has paid all other Taxes in respect of the Lessee's interest in Unit 2 and in the PVNGS Site which are payable by the Lessee to the extent the same have become due and payable and before they have become delinquent, except for (i) any Taxes the amount, applicability or validity of which may be in dispute and which are currently being contested in good faith by appropriate proceedings and with respect to which APS has set aside on its books reserves (segregated to the extent required by generally accepted accounting principles) deemed by it to be adequate and (ii) any Taxes relating to PVNGS in respect of which the Operating Agent has not given notice to APS that the same are due and payable. The Federal income tax returns of APS have been audited by the IRS for taxable years through December 31, 1982.

(15) ERISA. In reliance upon, and subject to the accuracy of, the representations made by the Equity Participant in Section 7(a)(9), the execution and delivery of this Participation Agreement and the other Transaction Documents to which the Lessee is a party will not involve any prohibited transaction within the meaning of ERISA or section 4975 of the Code.

(16) Regulation. So long as the Facility Lease is in effect, assuming the proper filing of Form U-7D with the SEC on or within 30 days after the Closing Date, under Applicable Law now in effect, neither any Loan Participant, the Equity Participant, FNB nor the Owner Trustee will be or

become, solely by reason of either its entering into this Participation Agreement or any other Transaction Document to which any of them is, or is to become on or before the Closing Date, a party, or the transactions contemplated hereby or thereby, subject to regulation (i) as an electric utility, a public utility or a holding company by any Federal or Arizona public utility commission or other regulatory body, authority or group (including, without limitation, the SEC, the FERC or the Arizona Corporation Commission) or (ii) in any manner by the NRC.

(17) Authorizations, etc. The Lessee has not failed to obtain any Governmental Action under any Federal or Arizona law or other authorization, license, approval, permit, consent, right or interest under any Federal or Arizona law, where a failure to obtain such would materially and adversely affect the ability of APS to carry on its business as presently conducted.

(18) No Default, etc. APS is not in default, and no condition exists that, with the giving of notice or lapse of time or both, would constitute a default by APS, under the Existing Mortgage or any other material mortgage, deed of trust, indenture, lease, contract or other instrument or agreement to which APS is a party or by which it or any of its properties or assets may be bound.

(19) Certain Documents. True and correct copies of the ANPP Participation Agreement, the Material Project Agreements and the Existing Mortgage have been delivered to counsel to the Equity Participant. No ANPP Project Agreement will, on and after the Closing Date, materially and adversely interfere with (i) except (in the case of the Generation Entitlement Share only) for the ANPP Participation Agreement, the title of the Owner Trustee to the Undivided Interest or the Real Property Interest, or (ii) except for the ANPP Participation Agreement, the use of, or the exercise by the Owner Trustee of its rights under the Facility Lease, the Real Property Interest, the Purchase Documents and the Assignment and Assumption with respect to, the Undivided Interest and the interests in the PVNGS Site (including the Real Property Interest) granted or to be granted under

the Purchase Documents and the Assignment and Assumption. No payment default or other default of a material nature by the Lessee has occurred and is continuing under the Existing Mortgage or any ANPP Project Agreement. Each of the ANPP Participation Agreement and the other ANPP Project Agreements is in full force and effect and no breach of any thereof, to the Lessee's knowledge, by any other party thereto has occurred and is continuing, except where the failure to be in force and effect or such breach would not have a material and adverse effect on the Undivided Interest (including the related Generation Entitlement Share), the Real Property Interest, Unit 2 or the rights, interest and benefits of the Owner Trustee or the Equity Participant under any Transaction Document. Upon execution and delivery of the Mortgage Release and the recordation thereof or of UCC releases in respect thereof, (i) the mortgagee and secured party thereunder will have released the lien of the Existing Mortgage on the Undivided Interest and (ii) the rights of the Owner Trustee in the Undivided Interest and the Real Property Interest will not be and will not become subject or subordinate to the rights of any Person, except the Indenture Trustee under the Indenture and the ANPP Participants under, and to the extent expressly set forth in, the ANPP Participation Agreement (as in effect on the Closing Date) and except as may otherwise expressly be permitted by the Facility Lease. The lien of the Existing Mortgage does not extend to rights of the Lessee under any Transaction Document (other than the Lessee's leasehold interest under the Facility Lease).

(20) Unit 2. The description of Unit 2 set forth in Exhibit B to the Bill of Sale, as delivered on the Closing Date, will be correct and sufficiently complete to identify such property.

(21) Investment Company Act. The Lessee (a) is not an "investment company", or a company "controlled" by an "investment company", within the meaning of the Investment Company Act and (b) is a "subsidiary company" of a "holding company", AZP Group, Inc., and an "affiliate" of a "holding company", as such terms are defined in the Holding Company Act, but is exempt from all provisions of the Holding Company Act and the rules thereunder

(except Section 9(a)(2) of the Holding Company Act).

(22) Sale and Conveyance. The sale and conveyance of the Undivided Interest, the Real Property Interest and any other property or interest in property transferred by APS under the Transaction Documents will not render APS insolvent nor is it being made in contemplation of APS's insolvency; the property remaining in the hands of APS after such sale, conveyance and transfer is not an unreasonably small capital; APS does not intend to or believe that it will incur debts beyond its ability to pay as they mature; and APS has no actual intent to hinder, delay or defraud either present or future creditors.

(b) Agreements.

(1) Delivery of Documents. The Lessee shall deliver to the Equity Participant and the Loan Participant (and, in the case of Sections 10(b)(1)(iii) and 10(b)(1)(iv), the Owner Trustee):

(i) Financial Statements: (A) as soon as practicable, and in any event within 120 days, after the end of each fiscal year of the Lessee, a consolidated balance sheet of the Lessee as of the end of such fiscal year and related consolidated statements of income, retained earnings and changes in financial position for such year, all in reasonable detail and certified in an opinion by a nationally recognized firm of independent public accountants, and the annual and interim reports of the Lessee to holders of its securities as soon as the same have been mailed to such holders, (B) as soon as practicable, and in any event within 60 days, after the end of each fiscal quarter (other than the last fiscal quarter) of each fiscal year of the Lessee, a consolidated balance sheet of the Lessee as of the end of said period and a related consolidated statement of income, retained earnings and changes in financial position for said period, all in reasonable detail, and certified by the Chief Financial Officer, the Controller or an Assistant

Controller, the Treasurer or an Assistant Treasurer of the Lessee and (C) as soon as practicable and in any event within 15 days of their being filed with the SEC, copies of all documents filed by the Lessee with the SEC pursuant to the reporting requirements of the Securities Exchange Act;

(ii) Other Reports: promptly upon their becoming available, any registration statement, offering statement, investment memorandum or prospectus prepared by the Lessee in connection with the public offering of securities (other than public offerings of securities under employee stock option, consumer stock or dividend reinvestment plans);

(iii) Notice of Default: promptly upon the Lessee becoming aware of the existence thereof, written notice specifying any condition which constitutes a Default, an Event of Default, an Indenture Default or an Indenture Event of Default or a default by any ANPP Participant under the ANPP Participation Agreement and, in each case, the nature and status thereof;

(iv) Annual Certificate: within 120 days after the end of each fiscal year of the Lessee, a certificate of the Lessee, signed by the Chief Financial Officer, the Controller, an Assistant Controller, the Treasurer or an Assistant Treasurer of the Lessee, to the effect that such officer has reviewed, or caused to be reviewed by individuals under his supervision, this Participation Agreement and each other Transaction Document and each Financing Document to which the Lessee is a party, and has made, or caused to be made, under his supervision, a review of the transactions contemplated hereby and thereby and the condition of the Lessee and its subsidiaries during such preceding fiscal year, and such review has not disclosed the existence during such fiscal period, nor does such officer have knowledge of the existence as at the date of such certificate, of any condition or event that constitutes a Default or Event of Default or, if any such condition or event

exists, specifying the nature and period of existence thereof and any action the Lessee has taken, is taking, or proposes to take with respect thereto;

(v) Opinion of Counsel: within 120 days after the end of each fiscal year of the Lessee, an opinion or opinions, satisfactory to the Equity Participant, the Owner Trustee, the Collateral Trust Trustee and the Indenture Trustee, of Snell & Wilmer, counsel for the Lessee, and/or other counsel acceptable to the Equity Participant (A) either to the effect that (1) all filings and recordations (or refilings and rerecordations) required to (i) convey to the Owner Trustee, and preserve the title of the Owner Trustee to, the Undivided Interest and the Real Property Interest, and (ii) so long as any Note is Outstanding, grant, perfect, and preserve the security interest of the Indenture Trustee in the Lease Indenture Estate have been duly made, or (2) no such additional filings, recordings, refilings or rerecordings are necessary, and (B) specifying the particulars of all action required during the period from the date of such opinion through the last day of the next succeeding calendar year, including, in the case of each UCC continuation statement required to be filed during such period, the office in which each such continuation statement is to be filed and the filing date and filing number of the original financing statement or fixture filing to be continued, and the dates within which such continuation statement may be filed under Applicable Law;

(vi) ANPP Information: upon receipt by the Lessee, unless prohibited by Applicable Law and subject to applicable confidentiality undertakings with respect thereto, copies of (A) minutes of all committee meetings of the ANPP Administrative Committee, the ANPP Engineering and Operating Committee, the ANPP Auditing Committee and other committees composed of the ANPP Participants, (B) all annual capital budgets, annual operation and maintenance budgets and monthly statistical reports on the operation of PVNGS, (C) all

notices to or from the NRC with respect to violations or other material occurrences with respect to PVNGS, and (D) Institute of Nuclear Power Operations evaluation reports;

(vii) Requested Information: with reasonable promptness, unless prohibited by Applicable Law, such other data and information as to the business and properties of the Lessee or as to Unit 2, PVNGS or the PVNGS Site as from time to time may be reasonably requested by the Equity Participant, subject, however, to applicable confidentiality undertakings with respect thereto.

(2) Further Assurances. The Lessee shall cause to be promptly and duly taken, executed, acknowledged and delivered all such further acts, documents and assurances as any Loan Participant, the Owner Trustee or the Equity Participant may from time to time reasonably request in order to carry out more effectively the intent and purposes of this Participation Agreement, the other Transaction Documents and any Financing Documents, and the transactions contemplated hereby and thereby. The Lessee shall cause the financing statements (and continuation statements with respect thereto) and the documents enumerated and described in Schedule 5, and all other documents necessary or advisable in that connection, to be recorded or filed at such places and times, and in such manner, and will take all such other actions or cause such actions to be taken, as may be necessary or reasonably requested by any Loan Participant, the Equity Participant, the Collateral Trust Trustee, the Owner Trustee or the Indenture Trustee, in order to establish, preserve, protect and perfect the title of the Owner Trustee to the Undivided Interest and the Real Property Interest and the Owner Trustee's rights and interests under this Participation Agreement and the other Transaction Documents and, so long as any Note is Outstanding, the first and prior security interest of the Indenture Trustee in the Lease Indenture Estate.

(3) Covenants.

(i) Maintenance of Corporate Existence, etc. The Lessee shall at all times maintain

its existence as a corporation under the laws of the State of Arizona, except as permitted by paragraph (ii) below (including any consent given by the Equity Participant pursuant to such paragraph (ii)), and qualify and remain qualified to do business in each jurisdiction where the conduct of its business or the ownership of its properties requires such qualification. The Lessee will do or cause to be done all things necessary to preserve and keep in full force and effect its material franchises; provided, however, that the Lessee may discontinue or permit the discontinuance of any material franchise if (x) its board of directors shall determine that such discontinuance is necessary or desirable in the conduct of its business and does not materially and adversely affect or diminish any right of the Equity Participant or any Loan Participant or (y) the Lessee continues to provide electric service to the area covered by such material franchise to the substantially same extent and on substantially the same terms and conditions as provided prior to such discontinuance pending the renegotiation or renewal thereof.

(ii) Merger, Sale, etc. Without the consent of the Equity Participant, each Loan Participant and the Indenture Trustee, the Lessee shall not (1) consolidate with any Person, (2) merge with or into any Person, or (3) convey or transfer to any Person more than 10% of its total assets, including cash (determined, in each case, on the basis of the values of such assets, as shown on the most recent certified balance sheet of the Lessee delivered to the Equity Participant pursuant to Section 10(b)(1)(i)(A)), in any single transaction or series of related transactions, unless, immediately after giving effect to such transaction:

(A) the Person who is the Lessee under the Facility Lease immediately following such consolidation, merger, conveyance or transfer (the Surviving Lessee) shall be a corporation which (i) is organized under the laws of the United

States of America, a state thereof or the District of Columbia, (ii) is a utility which is a principal supplier of electric service to residents of Phoenix, Arizona, (iii) is an ANPP Participant under the ANPP Participation Agreement with respect to Unit 2 (including the Undivided Interest), (iv) shall have assumed each covenant and condition of the Lessee under the ANPP Participation Agreement and each other ANPP Project Agreement, and (v) holds a valid and subsisting license from the NRC to possess Unit 2 (including the Undivided Interest);

(B) the Surviving Lessee, if other than the Lessee immediately prior to such transaction, shall execute and deliver to the Equity Participant and the Indenture Trustee an agreement, in form and substance reasonably satisfactory to the Equity Participant, containing the assumption by the Surviving Lessee of each covenant and condition of this Participation Agreement and each other Transaction Document to which the Lessee immediately prior to such transaction was a party immediately preceding such transaction;

(C) no Default (other than a failure to deliver documents and other information specified in Section 10(b)(1)(vi)), Event of Loss or Deemed Loss Event shall have occurred and no Event of Default shall have occurred and be continuing;

(D) for the benefit of the Equity Participant only, the Surviving Lessee, if other than the Lessee immediately prior to such transaction, shall have provided a Letter of Credit which meets the requirements set forth in Section 10(b)(3)(ix) to the Equity Participant in the same amount as was available immediately prior to such transaction;

(E) the Surviving Lessee shall have delivered to the Equity Participant and

the Indenture Trustee an Officers' Certificate and an opinion, reasonably satisfactory to the Equity Participant, of independent counsel to the Surviving Lessee, each stating that (1) such transaction complies with this paragraph (ii) and (2) all conditions precedent to the consummation of such transaction have been satisfied and any Governmental Action required in connection with such transaction has been obtained, given or accomplished;

(F) the Surviving Lessee shall have delivered to the Equity Participant an opinion, reasonably satisfactory to the Equity Participant, of independent counsel to the Surviving Lessee, stating that such transaction does not and will not cause a Tax Loss (as defined in the Tax Indemnification Agreement);

(G) such transaction is otherwise permitted by and is in compliance with the ANPP Participation Agreement;

(H) (i) the Surviving Lessee shall have a debt to equity ratio of not more than 3 to 1 or (ii) the long-term unsecured debt securities of the Surviving Lessee shall be rated at least "investment grade", as determined by Moody's and Standard & Poors, if the Lessee has long-term unsecured debt securities rated by such rating organizations, or as determined by one of such rating organizations, if the Surviving Lessee has long-term unsecured debt securities rated by only one such organization, or, if neither of such rating organizations shall rate such debt securities of the Surviving Lessee at the time, by any nationally recognized rating organization in the United States of America; and

(I) the Surviving Lessee shall have a Net Worth not less than \$1,400,000,000.

Upon the consummation of such transaction the Surviving Lessee, if other than the Lessee, shall succeed to, and be substituted for, and may exercise every right and power of, the Lessee immediately prior to such transaction under this Participation Agreement and each other Transaction Document and Financing Document to which the Lessee immediately prior to such transaction was a party immediately prior to such transaction, with the same effect as if the Surviving Lessee had been named herein and therein.

(iii) Change in Chief Executive Office.

The Lessee shall notify the Owner Trustee, the Equity Participant, each Loan Participant and the Indenture Trustee promptly after any change in the location of its chief executive office and place of business, principal place of business or place where the Lessee maintains its business records.

(iv) No Petition Agreement. Prior to the 181st day following the payment in full of any Bonds and the discharge in accordance with its terms of any Collateral Trust Indenture, the Lessee shall not file a petition, or join in the filing of a petition, seeking reorganization, arrangement, adjustment or composition of or in respect of Funding Corp under the Bankruptcy Code or any other applicable Federal or state law or the law of the District of Columbia.

(v) ANPP Project Agreements. Except where the failure to do so would not have a material and adverse effect on the Undivided Interest, the Real Property Interest, Unit 2 or the rights, interests and benefits of the Owner Trustee, the Equity Participant or any Loan Participant under any Transaction Document, the Lessee at all times, unless the Equity Participant shall otherwise consent, shall (1) perform its obligations under and comply with the terms of each ANPP Project Agreement to be complied with by it, (2) exercise its rights under the ANPP Participation Agreement to maintain each ANPP Project Agreement in full force and effect, (3) keep

unimpaired all of the Lessee's rights, powers and remedies under each ANPP Project Agreement and prevent any forfeiture or impairment thereof, (4) take such action as may be available to it to cause the enforcement of the ANPP Participation Agreement in accordance with its terms, (5) not take or fail to take or join in any action with respect to or accept or approve (A) any amendment to or any other change in, the ANPP Participation Agreement or any other ANPP Project Agreement, or (B) any other action or change, the effect of which would be to relieve the Lessee of any obligations under the ANPP Participation Agreement on or after the Closing Date and (6) not accept or approve any amendment to any ANPP Project Agreement the effect of which would be to (A) reduce the Generation Entitlement Share included in the Undivided Interest, (B) relieve the Lessee of any obligation under the ANPP Participation Agreement in respect of the Undivided Interest or the Real Property Interest on or after the Closing Date, (C) impose, directly or indirectly, on the Owner Trustee or the Equity Participant at any time any obligations, (D) discriminate against (x) the Owner Trustee or the Equity Participant in its capacity as lessor in a sale and leaseback transaction or (y) any present or future ANPP Participant because such ANPP Participant derived or will derive its status as "Participant" under the ANPP Participation Agreement from a lessor in a sale and leaseback transaction, or (E) deprive the Owner Trustee or the Equity Participant, as the case may be, of the benefit of Sections 15.2.2, 15.10 and 32.1 of the ANPP Participation Agreement (or any comparable successor provisions). The Lessee shall (X) provide copies of any proposed amendment to or modification of the ANPP Participation Agreement to the Equity Participant not less than 45 days prior to the execution thereof by the Lessee (except where the Lessee is unaware thereof 45 days prior to such execution, in which case the Lessee shall provide notice thereof as promptly as possible after becoming so aware) and (Y) upon such execution furnish to the Equity Participant and the Indenture

Trustee a copy of any such amendment or modification as executed.

(vi) Notes and Bonds. The Lessee will not, and will not permit any of its Affiliates to, acquire any of the Notes or the Bonds.

(vii) Cooperation. The Lessee shall accept and cooperate in receiving the Special Transfer, either on its own behalf or, if the Equity Participant so requires, on behalf of the Person designated by the Lessee to receive the Special Transfer. If at the time a Special Transfer is effected, the Lessee shall not have assumed all obligations under the Initial Series Notes, the provisions of Section 4(a) (and related definitional provisions) of the form of Bank Exchange Note shall at all times thereafter be incorporated herein by reference (except that "Company" shall be "Lessee") until all Initial Series Notes are paid in full.

(viii) Decommissioning. (A) Unit 2, the Common Facilities used in respect of Unit 2, the other property included in the Unit 2 Retained Assets and allocable to Unit 2 and the portion of the PVNGS Site allocable to Unit 2 shall be decommissioned and retired from commercial service in accordance with Applicable Law and, to the extent a method of decommissioning is not prescribed by Applicable Law, by the method for decommissioning determined as provided in the ANPP Participation Agreement (the foregoing being herein referred to as Decommissioning). (B) As between the Lessee, the Owner Trustee, the Equity Participant, each Loan Participant and any transferee (including by way of lease) or assignee of any of the Lessor's or the Equity Participant's right, title or interest in Unit 2, the Lessee agrees to pay, be solely responsible for, and to indemnify such parties against, all costs and expenses relating or allocable to, or incurred in connection with, Decommissioning to the extent of a 29.1% undivided interest in Unit 2 (all such costs and expenses being herein referred to as Decommissioning Cost), notwithstanding (i) the

occurrence of the Lease Termination Date, any Default, Event of Default, Event of Loss, Deemed Loss Event or any other event or occurrence, (ii) any provision of any Transaction Document, or other document, instrument or agreement, including the ANPP Participation Agreement, (iii) any provision of the License or any other license or permit, or (iv) any Applicable Law, either now or hereafter in effect, charter or by-law provision, Governmental Action or other impediment, including, without limitation, the bankruptcy or insolvency of the Lessee; it being understood that the obligations of the Lessee under this clause (B) are and shall be absolute and unconditional. (C) The Lessee shall use its best efforts to cause the ANPP Administrative Committee to use the safest and most reliable method of Decommissioning consistent with public health and safety. (D) The Lessee shall establish a special decommissioning trust fund or funds (the Decommissioning Trust Fund) for the accumulation and full funding of amounts sufficient by December 31, 2015 to pay Decommissioning Cost. For this purpose, Decommissioning Cost shall be as determined by an expert selected by the Equity Participant and reasonably acceptable to the Lessee (the Decommissioning Expert). For purposes of making such determination, such expert shall assume that the method of Decommissioning Unit 2 shall be the costlier of (i) the DECON method of decommissioning (if not prohibited by Applicable Law), plus cost of removal, or (ii) the method of decommissioning required under Applicable Law. The Decommissioning Trust Fund shall be created as promptly as practicable after the Closing Date by the execution and delivery of the Decommissioning Trust Agreement. The Decommissioning Trust Fund shall be funded by the making of semi-annual deposits in the Decommissioning Trust Fund (with the first such semi-annual deposit to be made on or before the fifth anniversary of the Closing Date) by the Lessee in such amounts as would, based on investments in such securities as are permitted under the Decommissioning Trust Agreement and utilizing the actuarial

assumptions used by the Lessee as of the Closing Date for its pension fund, as such assumptions may be changed from time to time by the Lessee with the consent of the Equity Participant, result in the Decommissioning Trust Fund being funded by December 31, 2015 in the full amount of the Decommissioning Cost; provided, however, that such actuarial assumptions shall reflect that earnings on amounts deposited in the Decommissioning Trust Fund shall be subject to Federal income taxation until such time that under Applicable Law such earnings on such amounts will not be subject to Federal income taxation. During the first 25 years after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert every five years. Commencing in the 26th year after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert each year. Immediately following each such determination by the Decommissioning Expert prior to December 31, 2015, the Lessee will make appropriate adjustments, if required, in its semi-annual deposits to be made thereafter so that, based on the investment and actuarial assumptions then in effect with respect to the Decommissioning Trust Fund, such Fund will be funded in the full amount of the Decommissioning Cost as so determined by December 31, 2015. During the first 20 years following the Closing Date, the Decommissioning Trust Fund will be invested and reinvested in accordance with standards no more liberal than the investment guidelines and actuarial assumptions set forth in the Decommissioning Trust Agreement. Commencing in the 21st year following the Closing Date and thereafter, the Decommissioning Trust Fund will be invested and reinvested in Decommissioning Fund Permitted Investments; provided, however, that in no event shall the Decommissioning Trust Fund be invested in any securities of the Lessee or any Affiliate thereof. The Decommissioning Trust Fund shall be the fund of the Lessee, provided that the Lessor shall be granted and shall have a security interest in such fund as security for the obligations of the Lessee under this

Section 10(b)(3)(viii). If, after the Decommissioning of Unit 2, there shall be any funds remaining in the Decommissioning Trust Fund, such funds shall be the property of, and be paid to, the Lessee. (E) In the event that (i) the Facility Lease shall have expired or terminated on or after December 31, 2015, (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default) and (ii) thereafter the Lessor shall (1) release the Undivided Interest to any Person or (2) retain the Undivided Interest and sell power and energy from its Generation Entitlement Share, then after the Lessor has received (x) in the case of clause (1) above, net rents (after reduction for expenses incurred by the Lessor in connection therewith) in an aggregate amount (when discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) equal to 23.5% of Facility Cost, as adjusted to reflect inflation or deflation from the Closing Date to the time of determination (the Adjusted Base Amount), or (y) in the case of clause (2) above, net electric revenues (after reduction for expenses incurred by the Lessor in earning such revenues) in an aggregate amount (discounted as aforesaid) equal to the Adjusted Base Amount, the Lessor shall thereafter reimburse the Lessee out of any further net rent received or net proceeds received from the sale of power and energy to the extent that such rent or proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2 (payable on an annual basis with respect to each year or portion thereof during the term of such lease referred to in clause (1) above or such period referred to in clause (2) above during which the Lessor retains the Undivided Interest); provided, however, that when such amount has been paid the Lessor shall have no further obligation to make reimbursement to the Lessee pursuant to this Section 10(b)(3)(viii). (F) In the event that (i) the Facility Lease

shall have expired or terminated on or after December 31, 2015 (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default), (ii) the Lessor shall sell the Undivided Interest to any Person (including the Lessee in connection with the exercise by the Lessee of the purchase option provided by Section 13(c) of the Facility Lease), and (iii) the net sales proceeds (discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) received by the Lessor in connection therewith shall exceed the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above), then the Lessor shall reimburse the Lessee out of the net proceeds of such sale, to the extent that such proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2, whereupon the reimbursement obligation of the Lessor under this Section 10(b)(3)(viii) shall terminate; provided, however, that any such reimbursement shall not reduce the amount of such net sales proceeds retained by the Lessor to an amount (discounted as aforesaid) equal to less than the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above). The reimbursement obligations of the Lessor under clauses (E) and (F) of this Section 10(b)(3)(viii) are for the the sole benefit of the Lessee, and no other Person shall be a third party beneficiary with respect thereto. For purposes of this Section 10(b)(3)(viii), (x) the amount of net rents, net revenues and net sales proceeds attributable to the decommissioning obligation of the Lessee shall be the amount by which such rents, revenues and proceeds are greater than they would have been if the Lessee had had no such obligation, and (y) the amount thereof attributable to the period after the Lease Termination Date shall be the amount determined in the immediately preceding clause

(x) multiplied by a fraction the denominator of which is the number of months in the period commencing May 20, 1986, and ending on the expiration of the economic useful life of Unit 2 as estimated at the time a determination is being made pursuant to this Section 10(b)(3)(viii) and the numerator of which is the number of months in the period commencing on the Lease Termination Date and ending on the expiration of such economic useful life. In the event that the Lessee and the Lessor shall not agree as to the amount of net rents, net electric revenues or net sales proceeds attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date, such amount shall be determined by the Appraisal Procedure. (G) Upon presentation of evidence by the Lessee, reasonably satisfactory to the Equity Participant and the Owner Trustee, that there are amounts then due to pay Decommissioning Cost, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to be delivered pursuant to the Decommissioning Trust Agreement for payment of Decommissioning Cost. (H) Upon presentation of a certificate of a nuclear expert selected by the Lessee and reasonably satisfactory to the Equity Participant and the Owner Trustee, stating that Decommissioning has been completed and all Decommissioning Cost has been paid in full, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to release any funds then remaining in the Decommissioning Trust Fund. (I) Notwithstanding anything in this Participation Agreement or any other Transaction Document to the contrary, the Equity Participant, the Owner Trustee and the Lessee agree to cooperate in amending this Participation Agreement and the Decommissioning Trust Agreement to the extent necessary to enable the Decommissioning Trust Agreement to comply with Section 468A of the Code, or to establish a separate fund meeting the requirements of said Section 468A; provided, however, that in no event shall any

such amendment have a material adverse effect on the Equity Participant's rights in Unit 2 or its security interest in the Decommissioning Trust Fund.

(ix) Letter of Credit. The Lessee shall cause Morgan Bank to issue in favor of the Equity Participant a Morgan Bank irrevocable, transferable letter of credit (such letter of credit and all letters of credit or other credit support instruments issued or executed from time to time in replacement thereof or as a renewal thereof being herein referred to as the Letter of Credit) which, for a term of five years, shall secure the Equity Participant for the payment of Rent due and payable by the Lessee from time to time under the Facility Lease to the extent of the amount available to be drawn under the Letter of Credit at such time. The original stated amount of the Letter of Credit provided by Morgan Bank on the Closing Date shall be \$45,259,626.31, which amount shall be reduced by the amount of each drawing thereunder and shall not be reinstated. The Lessee shall give the Equity Participant notice of the scheduled termination of the Letter of Credit not more than 90 nor less than 60 days before the scheduled termination date. The Lessee agrees to use its best efforts during the Basic Lease Term to renew or replace any expiring Letter of Credit prior to the expiration date thereof with an irrevocable, transferable, unsecured letter or letters of credit having an original stated term of not less than three and not more than eight years, issued by an Eligible Bank or Eligible Banks (the Issuing Bank), or with some other form of credit support acceptable to the Equity Participant in its sole judgment, so that at all times during the Basic Lease Term there shall be a Letter of Credit securing the payment of Rent due and payable by the Lessee from time to time under the Facility Lease to the extent of the amount available to be drawn under the Letter of Credit from time to time. The maximum amount available to be drawn under any replacement Letter of Credit shall be adjusted after each date on which Basic Rent

is due, it being understood, however, that such adjustment shall not take effect until at least ten days after each date on which Basic Rent is due. Any replacement Letter of Credit (1) shall permit partial drawings, (2) shall permit the Equity Participant to assign all or any part of its interest therein without the Issuing Bank's or the Lessee's consent and (3) shall not have termination provisions which are less favorable to the Equity Participant than those of the initial Letter of Credit issued by Morgan Bank. Any reimbursement agreement between the Lessee and the Issuing Bank relating to any replacement Letter of Credit (1) shall not have default provisions which are less favorable to the Lessee than those in the reimbursement agreement for the initial Letter of Credit from Morgan Bank, (2) shall require that the Issuing Bank pay any draws on the Letter of Credit from general funds, and (3) shall not permit the Issuing Bank to exercise its right to set off against any amounts owed as reimbursement to the Issuing Bank for draws on the Letter of Credit. The Lessee shall not grant or permit to exist any Lien on any of its property in favor of the Issuing Bank to secure reimbursement obligations of the Lessee to the Issuing Bank. The Lessee shall not amend any provision of the reimbursement agreement with respect to any Letter of Credit in a manner materially adverse to the interests of the Equity Participant without the prior written consent of the Equity Participant. In addition, if any Eligible Bank (other than Morgan Bank) has its long-term unsecured debt securities (or if it has no long-term unsecured debt securities rated, its long-term deposits) rated less than Aaa by Moody's at the time it issues a Letter of Credit, then if on any biannual anniversary of the date of issuance of such Letter of Credit the credit rating by Moody's of such Bank is below Aa3, within 90 days thereafter the Lessee shall replace such Letter of Credit with one issued by an Eligible Bank. If the Lessee has not secured a commitment for a renewal or replacement Letter of Credit on or prior to the 60th day preceding the stated

expiration date of the Letter of Credit then in effect, or within 10 days after any Issuing Bank shall have given not less than 30 days' notice of the termination of its Letter of Credit prior to its stated expiration date, the Lessee shall notify the Equity Participant of such fact and the Equity Participant shall have the opportunity to find a Person acceptable to it willing to issue a letter of credit for the account of the Lessee on substantially the same terms as the Letter of Credit then in effect, except that the annual fee payable under such replacement letter of credit may be up to 0.375% of the maximum drawable amount under the Letter of Credit. If the Equity Participant has not so found a Person on or prior to the 45th day preceding the stated expiration date of the Letter of Credit then in effect, or within 15 days after any Issuing Bank shall have given not less than 30 days' notice of the termination of its Letter of Credit prior to its stated expiration date, the Lessee shall, unless an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Event of Loss shall have occurred, have the right to purchase the Undivided Interest and the Real Property Interest at any time thereafter on or before the expiration date of the Letter of Credit (exercisable in the same manner as is provided in Section 16(e) of the Facility Lease) for a purchase price equal to the higher of (A) Extraordinary Casualty Value, determined as of the date of purchase, if such date of purchase is a date set forth in Schedule 5 thereto, or the date set forth in such Schedule immediately preceding such date of purchase, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from the date set forth in such Schedule to the date of purchase and (B) the Fair Market Sales Value thereof; provided, however, that if the Lessee shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued Bank Exchange Notes as therein provided), the principal amount of the Notes shall be deducted from the purchase price.

(x) Commercial Operation of Unit 2. On or before September 30, 1987, Unit 2 will have achieved an electric output of not less than 95% of an estimated rated capacity of 1,270 megawatts during a test period of at least 100 consecutive hours.

(xi) Certain Changes to ANPP Participation Agreement. If at any time, through the efforts of APS or otherwise, any of the restrictions on lessors contained in Sections 15.6.3 and 15.8 of the ANPP Participation Agreement are eliminated or reduced for or are made inapplicable to (through amendment, waiver or otherwise) any part of any Generating Unit or Capital Improvement (as such terms are defined in the ANPP Participation Agreement), APS shall cause such restrictions to be comparably eliminated or reduced or made inapplicable to the Lessor. The parties hereto agree to enter into such amendments to this Participation Agreement and the other Transaction Documents and such other instruments and documents as shall be necessary or appropriate to effect the foregoing.

(xii) Intentionally left blank.

(xiii) Limitation on Certain Rights of the Lessee. The Lessee shall not exercise any of its rights under Section 12(a), 12(b) or 13(c) of the Facility Lease unless it is concurrently exercising any similar rights it may have in any other facility leases relating to Unit 2. If the Lessee shall have elected to return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5(a) of the Facility Lease and subsequently determines prior to the Lease Termination Date that it requires additional capacity from PVNGS, before the Lessee concludes any arrangement for such capacity, it shall first give written notice to the Lessor. If the Lessor elects, within 30 days of receipt of such notice, to sell the Undivided Interest and the Real Property Interest to the Lessee, the Lessee shall purchase the Undivided Interest and the Real Property Interest at the Fair Market Sales

Value thereof (determined by agreement of the Equity Participant and the Lessee or, failing such agreement, by the Appraisal Procedure) on the Lease Termination Date. If the Lessor has not made such election prior to the expiration of the period during which the Lessor is entitled to make such election, the Lessee shall be free to conclude such arrangements for capacity from PVNGS as it desires.

(xiv) **Additional Financial Reports.** The Lessee shall provide, within 120 days after the end of the fiscal year of each ANPP Participant whose net worth is included in the calculation of Net Worth Factor, annual certified financial reports with respect to each such ANPP Participant.

(xv) **Other Agreements.** The Lessee shall not enter into or become bound by any agreement or arrangement which would proscribe its ability to assume the obligations and liabilities of the Owner Trustee in accordance with Section 3.9(b) of the Indenture or to accept the Special Transfer.

(xvi) **ANPP Agreements.** If for any reason any of the restrictions on lessors contained in Section 15.6.3, 15.8, or 15.10 of the ANPP Participation Agreement are applicable on the Lease Termination Date or the Lessee shall not have granted to the Lessor a ground lease as contemplated below by the Lease Termination Date, and the effect of such restriction or restrictions is to reduce the amount received by the Lessor upon a disposition (by sale, lease or otherwise) from what would have been realized had such restriction or restrictions not been applicable or had such ground lease been in effect, then the Lessee shall pay to the Lessor an amount equal to such reduction, payable within 10 days after determination of such amount. Such amount shall be determined promptly after the Lease Termination Date by agreement between the Equity Participant and the Lessee or, if they shall be unable to agree within 30 days after the Lease Termination Date, by the Appraisal Procedure.

(xvii) Ground Lease. APS shall use its best efforts to grant a ground lease to the Lessor covering the PVNGS Site (which shall provide for rent of \$1 per year until the expiration of the Lease Term and Fair Market Rental Value thereafter), in which case the Lessor shall simultaneously sell back to the Lessee the realty covered by the Deed for a price equal to the Real Estate Investment. The parties hereto will cooperate in effecting the foregoing.

SECTION 11. Conditions Precedent.

(a) Equity Participant and Agent Conditions. The obligation of (x) the Agent, for the account of the Original Loan Participants, to transfer title to the amount of funds on deposit in the Investment Account equal to the aggregate amount of Loans as contemplated by Section 2(c)(i) to the Indenture Trustee, for the account of the Owner Trustee, on the Closing Date, and (y) the Equity Participant to make the Investment on the Closing Date, shall be subject to the fulfillment, on or prior to the Closing Date, of the following conditions precedent (each instrument, document, certificate, opinion, policy or other writing referred to below to be in form and substance satisfactory to the Agent and the Equity Participant):

(1) Notice of Closing; Transaction Documents. Each shall have received executed copies, or sets of executed counterparts, of the Notice of Closing, each Transaction Document (other than the Tax Indemnification Agreement), the Mortgage Release and such other documents as are contemplated by this Participation Agreement, including the Purchase Documents.

(2) Notice of Amount of Loans. The Agent shall have received from Lessee a certificate specifying the actual aggregate amount of the Loans to be funded at Closing.

(3) Tax Indemnification Agreement. The Equity Participant shall have received an executed copy of the Tax Indemnification Agreement.

(4) Authentication Request, etc. The Owner Trustee shall have delivered to the Indenture

Trustee (x) a request, dated the Closing Date, authorizing the Indenture Trustee to authenticate and deliver to the Agent the Initial Series Notes upon the transfer of the amount of funds on deposit in the Investment Account equal to the aggregate amount of Loans as contemplated by Section 2(c)(i) hereof to the Indenture Trustee, for the account of the Owner Trustee, and (y) the counterpart of the Facility Lease marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART".

(5) Due Authorization, Execution and Delivery. All of the documents described in clauses (1) and (3) of this Section 11(a) shall have been duly authorized, executed and delivered by the respective parties thereto and shall be in full force and effect on the Closing Date, and the Agent and the Equity Participant shall have received evidence as to such authorization, execution and delivery.

(6) Initial Series Notes Transaction; Investment. In the case of the Agent, (A) the Owner Trustee shall have executed, and the Indenture Trustee shall have authenticated and delivered to the Agent, the Initial Series Notes in the respective principal amounts and registrations requested by the Agent and evidencing the Loans made on the Closing Date, and (B) the Equity Participant shall have made the Investment.

(7) Loan. In the case of the Equity Participant, the Agent, on behalf of the Original Loan Participants, shall have made the Loans.

(8) ANPP Administrative Committee. The ANPP Administrative Committee shall have made the finding required by Section 15.6.2 of the ANPP Participation Agreement.

(9) No Violation. The making by the Equity Participant of the Investment and by the Original Loan Participants of the Loans shall not violate any Applicable Law.

(10) No Default. No Default, Event of Default or, in the case of the Agent, Indenture Default or Indenture Event of Default, shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred.

(11) Recording and Filing. The recordations and filings described in Schedule 5 shall have been duly made and all recording and filing fees with respect thereto shall have been paid.

(12) Representations and Warranties of the Equity Participant. The representations and warranties of the Equity Participant set forth in Section 7(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent shall have received a certificate of an officer of the Equity Participant, dated the Closing Date, to such effect.

(13) Opinion of the Equity Participant's Special Counsel. In the case of the Agent, it shall have received a favorable opinion of Cravath, Swaine & Moore, as special counsel for the Equity Participant, dated the Closing Date and addressed to the Agent, in form and substance satisfactory to the Agent.

(14) Representations and Warranties of the Owner Trustee. The representations and warranties of FNB and the Owner Trustee set forth in Section 8(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent and the Equity Participant shall have received a certificate of an officer of FNB and a certificate of the Owner Trustee, dated the Closing Date, to such effect.

(15) Opinion of the Owner Trustee's Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Csaplar & Bok, as counsel for the Owner Trustee, dated the Closing Date and addressed to the Agent and the Equity Participant, in form and substance satisfactory to the Agent and the Equity Participant.

(16) Representations and Warranties of the Indenture Trustee. The representations and warranties of Chemical and the Indenture Trustee set forth in Section 9(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Agent and the Equity Participant shall have received a certificate of an officer of Chemical and the

Indenture Trustee, dated the Closing Date, to such effect.

(17) Opinion of the Equity Participant's Special NRC Counsel. The Equity Participant shall have received a favorable opinion of Shaw, Pittman, Potts & Trowbridge, as special NRC counsel for the Equity Participant, dated the Closing Date and addressed to the Equity Participant, in form and substance satisfactory to the Equity Participant.

(18) Representations and Warranties of the Lessee. (A) The representations and warranties of the Lessee set forth in Section 10(a), in any other Transaction Document, and in any certificate or other document to which the Lessee is a party, executed or delivered in connection with the transactions contemplated hereby or thereby, shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date and (B) no Deemed Loss Event or Event of Loss shall have occurred and no Default or Event of Default shall have occurred and be continuing and the Agent and the Equity Participant shall have received an Officers' Certificate of the Lessee, dated the Closing Date, to such effect, and to the further effect that (x) there has been no material adverse change in the properties, business, prospects or financial condition of the Lessee since June 30, 1986, and no event has occurred since that date which would materially adversely affect the ability of the Lessee to perform its obligations under this Participation Agreement or any other Transaction Document to which it is, or is to be, a party, and (y) there has been no material adverse change or development since June 30, 1986 relating to Unit 2, PVNGS or to nuclear power plants generally which affects the operations of Unit 2 or the value of the Undivided Interest or the financial condition of the Lessee.

(19) Opinion of the Lessee's Special Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, as special counsel for the Lessee, dated the Closing Date and addressed to each such Person, in form and substance satisfactory to the Agent and the Equity Participant.

(20) Opinion of Lessee's Counsel. The Agent and the Equity Participant shall have received a favorable opinion of Snell & Wilmer, as counsel to the Lessee dated the Closing Date and addressed to each such Person, in form and substance satisfactory to the Agent and the Equity Participant.

(21) Opinion of Equity Participant's Special Arizona Counsel. The Equity Participant shall have received a favorable opinion of Meyer, Hendricks, Victor, Osborn & Maledon, dated the Closing Date and addressed to the Equity Participant, in form and substance satisfactory to the Equity Participant.

(22) Opinion of the Equity Participant's Special Tax Counsel. The Owner Participant shall have received a favorable opinion of Shearman & Sterling, dated the Closing Date and addressed to the Equity Participant, with respect to such Federal tax and other tax matters as the Equity Participant may reasonably request.

(23) Opinion of Agent's Counsel. The Agent shall have received a favorable opinion of Morrison & Foerster, dated the Closing Date and addressed to it, in form and substance satisfactory to the Agent.

(24) Representations and Warranties of Funding Corp.. The representations and warranties of Funding Corp set forth in Section 6(a) shall be true and correct on and as of the Closing Date with the same effect as though made on and as of the Closing Date, and the Equity Participant shall have received an Officers' Certificate of Funding Corp, dated the Closing Date, to such effect.

(25) Opinion of Funding Corp's Counsel. Funding Corp shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, dated the Closing Date and addressed to it, in form and substance satisfactory to Funding Corp.

(26) Taxes. All Taxes, if any, payable in connection with the execution, delivery, recording and filing of the Transaction Documents and all the documents and instruments described in Schedule 5, or in connection with the issue and sale of the Initial Series Notes and the making by the Equity

Participant of the Investment and the Real Estate Investment, and all Taxes payable in connection with the consummation of the transactions contemplated hereby and by the other Transaction Documents, shall have been duly paid in full.

(27) Appraisals. The Equity Participant and the Agent shall have received a letter, dated the Closing Date and addressed to the Equity Participant, from Ebasco Business Consulting Company, containing an appraisal of the Undivided Interest, which appraisal shall reflect such appraiser's reasonable conclusion that (w) the fair market value in the hands of the Owner Trustee of the Undivided Interest on the Closing Date, taking into account the effect and existence of the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, is equal to not less than the Purchase Price as set forth in the Notice of Closing, (x) the estimated remaining economic useful life of Unit 2 and of the Undivided Interest is at least 39.309 years, (y) at the expiration of the first 2 years of the Fixed Rate Renewal Term the Undivided Interest will have an estimated residual value, taking into account the effect and the existence of this Participation Agreement, the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, in the hands of the Owner Trustee or a Person (unrelated to the Lessee) who could lease or purchase the Undivided Interest from the Owner Trustee for commercial use, equal to at least 20% of the Purchase Price, determined without including in such value any increase or decrease for inflation or deflation during the period from the Closing Date through the expiration of the first 2 years of the Fixed Rate Renewal Term, and (z) taking into account the effect and the existence of the Real Property Interest, the Assignment and Assumption and the ANPP Participation Agreement, the use of the Undivided Interest at the Lease Termination Date by any User is feasible from an engineering and economic point of view and is commercially reasonable. The Equity Participant shall have received an appraisal of the Real Property Interest, which appraisal shall reflect the appraiser's reasonable conclusion that the fair market value in the hands of the Owner Trustee of the Real Property Interest on the Closing Date is equal to the Real Estate Investment as set

forth in the Notice of Closing and shall cover such other matters as the Equity Participant shall have requested. The Equity Participant shall have received a letter from Ebasco Business Consulting Company discussing certain matters relating to the value of the Common Facilities and the Undivided Interest.

(28) Offering and Sale of Interest. The Agent, the Owner Trustee and the Equity Participant shall have received a letter from The First Boston Corporation and Lease Management Corporation with respect to the offering and sale of the interests in the transactions contemplated by this Participation Agreement.

(29) Governmental Action. The Lessee shall have obtained all Governmental Actions (including, without limitation, the Arizona Order, which order shall be final and non-appealable, and the License Amendment) required or, in the opinion of the Equity Participant and the Agent, advisable for the consummation of all the transactions contemplated by this Participation Agreement and the other Transaction Documents in accordance with their respective terms.

(30) Title Report; Title Insurance. The Equity Participant and the Agent shall have received (i) an updated title report, dated the Closing Date, with respect to the PVNGS Site, which report does not disclose any exceptions materially adverse to the possession or operation of Unit 2 or the performance by the Lessee of its obligations under this Participation Agreement and the other Transaction Documents to which the Lessee is a party; and (ii) such title insurance policies with respect to the PVNGS Site and improvements thereon (including the Owner Trustee's interests therein) as it shall have reasonably requested, such policies to be in form and substance satisfactory to the Equity Participant and the Agent.

(31) No Change or Proposed Change in Tax Laws. No change shall have occurred or been proposed in the Code or any other tax statute, the regulations thereunder or any interpretation thereof that would adversely affect the accuracy of the Tax Assumptions unless such change or proposed change relates to an

alternative minimum tax or the effect of such change or proposed change is provided for in Section 3(d) of the Facility Lease.

(32) Insurance. The Equity Participant shall have received a written report from its independent insurance consultant in form and substance satisfactory to the Equity Participant and a copy thereof shall have been delivered to Agent.

(33) Survey. The Equity Participant and Agent shall have received a survey of the PVNGS Site prepared subsequent to January 1, 1979.

(34) Special Certificate of the Lessee. The Equity Participant and the Agent shall have received a certificate of the Lessee, dated the Closing Date, to the effect that (A) Unit 2 has been in all material respects completed in a good and workmanlike manner and in accordance with the plans and specifications relating thereto (as the same may have been modified from time to time to reflect Unit 2 as actually completed), Applicable Law (including, without limitation, the regulations of the NRC), the License and the ANPP Participation Agreement, (B) all Governmental Actions necessary for the commercial operation of Unit 2 (including the Undivided Interest) have been received, other than any such Governmental Action that is routine in nature for PVNGS or that cannot be obtained under Applicable Law, or is typically not applied for, prior to the time it is required, and that the Lessee reasonably expects to be obtained in due course, (C) the plans and specifications relating to Unit 2 are complete in all material respects (modified or to be modified as aforesaid) and consistent with prudent engineering practice, (D) the testing and startup procedures and the operation and maintenance programs for Unit 2 are consistent with such plans and specifications, Applicable Law and prudent engineering practice, (E) Unit 2 has been tested in accordance with all customary testing and startup procedures which would have been performed on or prior to the Closing Date, and such tests and procedures indicate that Unit 2 will have the capacity and functional ability to perform in commercial operation, on a continuing basis, the function for which it is designed in accordance with such plans and specifications and has a nominal capacity of 1,270 megawatts electric,

(F) all material Governmental Actions relating to the construction, operation or maintenance of Unit 2 are listed in a schedule thereto, (G) there is no present event or condition which would materially adversely affect the capability of Unit 2 to operate in accordance with such plans and specifications and (H) based upon the Lessee's present reasonable expectations, and subject to Applicable Law, the rights and interests made available to the ANPP Participants (including the Lessee) pursuant to the ANPP Participation Agreement, as such rights and interests are made available or are to be made available to the Owner Trustee (or to any successor or assign of the Owner Trustee or any "Transferee" of the Owner Trustee under Section 15.10 of the ANPP Participation Agreement) under and pursuant to this Participation Agreement, the Real Property Interest or the Assignment and Assumption, together with the rights to be made available under and pursuant to the Assignment and Assumption, are adequate to permit, during the period following the Lease Termination Date or the taking of possession of the Undivided Interest and the Real Property Interest in the exercise of remedies under Section 16 of the Facility Lease, in accordance with the ANPP Project Agreements (i) the construction, location, occupation, connection, maintenance, replacement, renewal, repair or removal of Unit 2, (ii) the use, operation and possession of Unit 2, (iii) the construction, use, operation, possession, maintenance, replacement, renewal and repair of all Capital Improvements, (iv) adequate ingress to and egress from Unit 2 for any reasonable purpose in connection with the exercise of rights under the Assignment and Assumption and the ownership and possession of the Undivided Interest and (v) the obtaining of nuclear fuel, of water and of transmission services to the ANPP Switchyard sufficient to enable delivery of the Generation Entitlement Share included in the Undivided Interest in a commercially efficient manner and on commercially reasonable terms. Nothing in the foregoing clause (H) shall be deemed to be or be construed as a warranty by the Lessee as to the performance by the Operating Agent of its obligations under the ANPP Participation Agreement. Such certificate shall also be attested to by Edwin E. Van Brunt, Jr., Executive Vice President, of the Lessee, who shall state that (i) as a qualified engineer, he has made such investigation, inspection

and review as he deems necessary to make the statements in such certificate and (ii) to the best of his knowledge, the statements of the Lessee in such certificate are true and correct.

(35) Other Matters. The Agent and the Equity Participant shall have received such other documents, certificates and opinions as the Agent or the Equity Participant, or their respective counsel, shall reasonably request.

(b) Lessee Conditions. The obligation of the Lessee to sell and lease back the Undivided Interest and the Real Property Interest on the Closing Date pursuant to Section 4 shall be subject to the fulfillment or waiver on or prior to the Closing Date of the following conditions precedent, in each case in form and substance satisfactory to the Lessee:

(1) Paragraph (a) Documents. The Lessee shall have received copies of the documents, certificates, opinions (other than the opinion referred to in Section 11(a) (22)), appraisals, letters and forms described in paragraph (a) of this Section 11. All such opinions shall be addressed to the Lessee, except the opinions referred to in clauses (13), (15), (17), (19), (20), (21), (22) and (23) of said paragraph (a).

(2) Payment of Purchase Price. The Owner Trustee shall have paid to the Lessee an amount, in immediately available funds, equal to the Purchase Price and the Real Property Investment.

(3) Special Opinion of the Lessee's Special Counsel. The Lessee shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, dated the Closing Date and addressed to the Lessee, with respect to such Federal tax and other matters as the Lessee may reasonably request.

(4) Accountant's Letter. The Lessee shall have received a letter satisfactory to it from Deloitte Haskins & Sells, to the effect that, under generally accepted accounting principles and SFAS No. 13, the Facility Lease is an "operating lease".

(5) Order and License Amendment. The Arizona Order and the License Amendment shall be in form and

substance satisfactory to the Lessee and the Arizona Order shall be final and nonappealable.

(c) Conditions to Refundings. In addition to the limitations set forth in Section 2(e), the obligation of the Equity Participant and Funding Corp to participate in a refunding or reoptimization of the any Outstanding Notes, as provided in Section 2(e) or 2(f), shall be subject to the fulfillment on or before the applicable Refunding Date of the following conditions precedent (each instrument, document, certificate, opinion or other writing to be in form and substance satisfactory to Funding Corp and the Equity Participant):

(1) Authentication Request, etc. The Owner Trustee shall have delivered to the Indenture Trustee a request, dated the applicable Refunding Date, authorizing the Indenture Trustee to authenticate and deliver the Refunding Notes to or upon the order of the Loan Participant against redelivery of the Outstanding Notes to the Indenture Trustee for cancellation.

(2) Refunding Notes and Bond Transactions. (A) The Loan Participant shall have received (x) if and to the extent that the Loan Participant is Funding Corp, the proceeds from the sale of Refunding Bonds in an amount sufficient to make the Refunding Loan, and (y) from the Lessee (as a special payment of Basic Rent, if the Refunding Date shall be a date other than June 30 or December 30 of any year), an amount equal to accrued interest on the Outstanding Notes from, and including, the later of the date thereof or the date to which interest thereon shall have been paid, to, but excluding, the applicable Refunding Date, (B) the Owner Trustee shall have executed, and the Indenture Trustee shall have authenticated and delivered, to or upon the order of the Loan Participant the Refunding Notes evidencing the Refunding Loan and (C) if and to the extent that the Loan Participant is Funding Corp, the Collateral Trust Trustee shall have accepted the Refunding Supplemental Indenture subjecting the Refunding Notes to the lien of the Collateral Trust Indenture.

(3) No Default. No Default, Event of Default, Indenture Default or Indenture Event of Default

shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred.

(4) Representations and Warranties. The representations and warranties of the Equity Participant, FNB and the Owner Trustee, and the Lessee set forth in Sections 7(a), 8(a) and 10(a), respectively, shall be true and correct on and as of the applicable Refunding Date with the same effect as though made on and as of such Refunding Date (with all references to the Closing Date in such representations and warranties being changed to a reference to the applicable Refunding Date), and the Loan Participant and the Equity Participant shall have received appropriate certificates, dated the Refunding Date, to such effect (and with respect to paragraph (3) above, in the case of the Lessee) and the Equity Participant, FNB, the Owner Trustee and the Lessee shall provide such additional representations and warranties as of the applicable Refunding Date as the Equity Participant, FNB, the Owner Trustee or the Lessee shall reasonably request.

(5) Registration Statement. If and to the extent that the Loan Participant is Funding Corp, and the Bonds shall be sold in a public offering, the Equity Participant and the Agent, if the Initial Series Notes are being refunded, shall have received an Officers' Certificate of the Lessee, dated the applicable Refunding Date, to the effect that on the date it becomes effective and on the applicable Refunding Date, the Registration Statement did not and does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements contained therein in light of the circumstances under which they were made not misleading.

(6) Opinions of Counsel. The Equity Participant, the Loan Participant and the Lessee shall have received a favorable opinion of Mudge Rose Guthrie Alexander & Ferdon, as counsel for Funding Corp, dated the Refunding Date and addressed to the Equity Participant, the Owner Trustee, the Indenture Trustee and the Lessee, addressing such matters relating to the transactions in connection with the Refunding Notes as the Equity Participant, the Owner Trustee, the Indenture Trustee or the Lessee may reasonably request. The Equity

Participant shall have received favorable opinions of Cravath, Swaine & Moore, as special counsel for the Equity Participant, Csaplar & Bok, as counsel for the Owner Trustee, Mudge Rose Guthrie Alexander & Ferdon, as special counsel for the Lessee, and Snell & Wilmer, as counsel for the Lessee, each dated the applicable Refunding Date and addressing such matters relating to the transactions in connection with the Refunding Notes as the Loan Participant, the Equity Participant, the Owner Trustee, the Indenture Trustee or the Lessee may reasonably request. The Equity Participant shall have also received an opinion of independent tax counsel, dated the Refunding Date and addressed to the Equity Participant, that the issuance of the Refunding Notes shall not result in any adverse tax effect to the Equity Participant.

(7) Receipt of Documents. If and to the extent that the Loan Participant is Funding Corp, Funding Corp and the Collateral Trust Trustee shall have received copies of all documents previously delivered to the Agent pursuant to Section 11(a).

(8) Satisfaction of Underwriting Agreement Conditions. If and to the extent that the Loan Participant is Funding Corp, all of the conditions precedent to Funding Corp's obligations under any Underwriting Agreement shall have been met or waived by Funding Corp.

(9) Amendments to Documents. The Equity Participant and the Lessee shall have amended the Tax Indemnification Agreement, and the Owner Trustee and the Lessee shall have amended the Facility Lease, so as to take into account the tax treatment of interest (including original issue discount) payable on any Refunding Note or Bond in a manner that is mutually acceptable.

SECTION 12. Consent to Assignment of the Facility Lease; Consent to Indenture.

(a) Consent to Assignment of Facility Lease. The Lessee hereby acknowledges, and consents in all respects to, the assignment of the Facility Lease by the Owner Trustee to the Indenture Trustee under and pursuant to the Indenture and agrees:

(i) to make each payment of Basic Rent and Supplemental Rent due or to become due thereunder to the extent constituting Assigned Payments (excluding, in any event, all Excepted Payments) directly to the Indenture Trustee at the Indenture Trustee's Office, so long as any of the Notes shall be Outstanding and unpaid; and

(ii) not to seek to recover any payment (other than a payment that both the Owner Trustee and the Lessee agree was made in mistake) made to the Indenture Trustee in accordance with the Indenture once such payment is made.

(b) Consent to Indenture. The Lessee hereby consents in all respects to the execution and delivery of the Indenture, and to all of the terms thereof, and the Lessee acknowledges receipt of an executed counterpart of the Indenture; it being understood that such consent shall not be construed to require the Lessee's consent to any future supplement to, or amendment, waiver or modification of the terms of, the Indenture or any Note, except to the extent expressly provided for.

SECTION 13. Lessee's Indemnities.

(a) General Indemnity. The Lessee agrees, whether or not any of the transactions contemplated hereby shall be consummated and whether or not the Facility Lease, any other Transaction Document or any Financing Document shall have expired or have been terminated, to assume liability for, and the Lessee does hereby agree to indemnify, protect, defend, save and keep harmless each Indemnitee, on an After-Tax Basis, from and against, any and all Claims which may be imposed on, incurred by or asserted against any Indemnitee (whether because of an act or omission by such Indemnitee or otherwise and whether or not such Indemnitee shall also be indemnified as to any such Claim by any other Person) in any way relating to or arising out of (i) Unit 2, the Undivided Interest, the Real Property Interest, PVNGS or the PVNGS Site, or any part of any thereof, any ANPP Project Agreement, the issuance or payment of the Bonds or the Notes, this Participation Agreement or any other Transaction Document or any Financing Document (including, without limitation, the performance or enforcement of any of the

obligations and terms hereunder or thereunder), (ii) a disposition of all or any part of the Undivided Interest, the Real Property Interest, Unit 2 or any other interest of the Owner Trustee in connection with any termination of the Facility Lease, or (iii) the design, construction, assembly, manufacture, financing, erection, purchase, acceptance, rejection, ownership, acquisition, delivery, redelivery, nondelivery, transportation, insuring, lease, sublease, preparation, installation, repair, rebuilding, improvement, modification, transfer of title, abandonment, possession, repossession, use, operation, maintenance, condition, sale, return, storage or disposition of the Undivided Interest, Unit 2, the Real Property Interest, any Capital Improvement, the PVNGS Site, any other facilities or property in or on the PVNGS Site or any other interest of the Owner Trustee or the Equity Participant in any thereof or any accident, nuclear incident or extraordinary nuclear occurrence in connection with any thereof (including, without limitation, (A) claims or penalties arising from any violation of law or liability in tort (strict, absolute or otherwise) or from the active or passive negligence of any Indemnatee, (B) loss of or damage to any property or the environment or death or injury to any Person, (C) latent and other defects, whether or not discoverable, (D) any claim for patent, trademark, service-mark or copyright infringement and (E) any claim of any Indemnatee incurred in the administration of this Participation Agreement, any other Transaction Document or any Financing Document and not paid as Transaction Expenses or included in Facility Cost and, if not included in Transaction Expenses, the reasonable fees and disbursements of counsel (including reasonable allocated costs of in-house counsel) and other professionals incurred in connection therewith); provided, however, that the Lessee shall not be required to indemnify any Indemnatee pursuant to this Section 13(a), (1) for any Claim in respect of Unit 2, the Undivided Interest or the Real Property Interest arising from acts or events not attributable to either any act or omission of the Lessee, whether as agent for such Indemnatee or otherwise, or the period on or before the Lease Termination Date, which occur after redelivery of the Undivided Interest and the Real Property Interest to the Owner Trustee in accordance with Section 5 of the Facility Lease, except to the extent expressly provided in any Transaction Document, the ANPP Participation Agreement or any other agreement or undertaking of the Lessee, (2) for any Claim against such Indemnatee

resulting solely from acts which would constitute the willful misconduct or gross negligence of such Indemnatee (unless imputed to such Indemnatee by reason of Unit 2, the Undivided Interest, the Real Property Interest, PVNGS, the PVNGS Site or any other facilities at the PVNGS Site or any occurrence in connection with any thereof or by reason of any act or omission of the Lessee whether as agent for such Indemnatee or otherwise), (3) for any Transaction Expense to be paid by the Owner Trustee pursuant to Section 14(a), (4) for any Claim resulting solely from a transfer by the Owner Trustee or the Equity Participant of all or part of its interest in the Facility Lease, Unit 2, the Real Property Interest or the Undivided Interest other than in connection with any early termination of the Facility Lease or any exercise of remedies under Section 16 thereof or the transfer contemplated by Section 7(b)(4) or the first transfer by the Equity Participant to an Affiliate of the Equity Participant or (5) in the case of any Loan Participant, the Indenture Trustee and the Collateral Trust Trustee, for any Claim based upon an untrue statement or alleged untrue statement or omission or alleged omission in the Registration Statement or any document or agreement in connection with the sale of the Bonds which is based upon information furnished to the Lessee or its agents by such Indemnatee expressly for use therein. To the extent that an Indemnatee in fact receives indemnification payments from the Lessee under the indemnification provisions of this Section 13(a), the Lessee shall be subrogated, to the extent of such indemnity paid, to such Indemnatee's rights with respect to the transaction or event requiring or giving rise to such indemnity, but only so long as such subrogation shall not materially adversely affect the rights of such Indemnatee or any other Indemnatee hereunder. Nothing herein or elsewhere contained shall be construed as constituting a guaranty by the Lessee of the principal of, premium, if any, or interest on the Notes or the Bonds or of the residual value or useful life of the Undivided Interest.

(b) General Tax Indemnity.

(1) Indemnity. All payments by the Lessee in connection with the transactions contemplated by the Transaction Documents shall be free of withholdings of any nature whatsoever (and at the time that the Lessee is required to make any payment upon which any withholding is required, the Lessee shall pay an

additional amount such that the net amount actually received by the Person entitled to receive such payment will, after such withholding, equal the full amount of the payment then due) and shall be free of expense to each Indemnatee for collection or other charges. If, for any reason, the Lessee is required to make any payment to a taxing authority with respect to, or as a result of, any withholding tax imposed on an Indemnatee by way of withholding from payments to such Indemnatee in respect of the transactions contemplated by the Transaction Documents, which withholding tax is not the responsibility of the Lessee under this Section 13(b) as determined pursuant to this Section 13(b) but without regard to the immediately preceding sentence of this Section 13(b)(1), then such Indemnatee shall pay to the Lessee on an After-Tax Basis an amount which equals the amount paid by the Lessee with respect to, or as a result of, such withholding tax. Whether or not any of the transactions contemplated hereby are consummated, except as provided in Section 13(b)(2), the Lessee shall pay, and shall indemnify, defend and hold each Indemnatee harmless, on an After-Tax Basis, from and against, any and all Taxes howsoever imposed (whether imposed on or with respect to the Indemnatee, the Lessee, Unit 2, the Undivided Interest, the Retained Assets, the Real Property Interest, any Capital Improvement or the PVNGS Site or any part thereof or interest therein or otherwise) by any Federal, state or local government or subdivision thereof or taxing authority in the United States of America or by any foreign country or subdivision thereof or by any foreign or international taxing authority in connection with or relating to (A) the design, construction, financing, purchase, acquisition, acceptance, rejection, delivery, nondelivery, transportation, ownership, assembly, possession, repossession, operation, use, condition, maintenance, repair, improvement, sale, return, storage, abandonment, redelivery, manufacture, insuring, leasing, subleasing, modification, transfer of title, rebuilding, rental, importation, exportation or other application or disposition of, or the imposition of any Lien other than, in the case of the Equity Participant, Equity Participant's Liens and, in the case of the Lessor, Lessor's Liens (or incurrence of any liability to refund or pay over any amount as a result of any Lien other than Equity Participant's Liens and Lessor's Liens) on,

Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof or interest therein, (B) the payment of Rent or the receipts or earnings arising from or received with respect to, and the indebtedness with respect to, Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof, interest therein or application or disposition thereof, (C) any amount paid or payable pursuant to this Participation Agreement, any other Transaction Document or any Financing Document or the transactions contemplated hereby or thereby, (D) Unit 2, the Undivided Interest, the Real Property Interest, the Retained Assets, any Capital Improvement or the PVNGS Site, or any part thereof, or interest therein, or the applicability of the Facility Lease to the Undivided Interest or any Capital Improvement, or any part thereof or interest therein, (E) this Participation Agreement, any other Transaction Document or any Financing Document or (F) otherwise with respect to or in connection with the transactions contemplated by this Participation Agreement, any other Transaction Document or any Financing Document.

(2) Exclusions from General Tax Indemnity.
Section 13(b)(1) (except for the first two sentences thereof) shall not apply to:

(i) Taxes based on, or measured by, net income of an Indemnatee imposed on such Indemnatee by the United States (including, without limitation, any minimum Taxes, capital gains Taxes, any Taxes on, or measured by, items of tax preference, surcharges, additions to tax, penalties, fines or other charges in respect thereof);

(ii) Taxes (other than sales, use or rental Taxes) imposed on an Indemnatee by any state or local government or any subdivision thereof or other taxing authority in the United States or by any foreign country or subdivision thereof or by any foreign or international taxing authority that are based on, or measured by, the net income, items of tax preference, net worth or capital of such

Indemnatee (Income/Capital Taxes), except, with respect to the Equity Participant and any Affiliate thereof and the Trust Estate, any such Income/Capital Taxes imposed by a jurisdiction as a result of a relation or asserted relation of such jurisdiction to the transactions contemplated by the Transaction Documents or the Financing Documents or as a result of the activities of the Lessee, any ANPP Participant or any Affiliate of any thereof in such jurisdiction; provided, however, that the amount of any Income/Capital Taxes for which the Lessee is obligated to indemnify under the preceding exception shall be calculated on a pro forma basis as the amount by which:

(x) the incremental Income/Capital Taxes which the Indemnatee is obligated to pay in such jurisdiction, calculated as:

(1) the actual amount of Income/Capital Taxes which the Indemnatee is obligated to pay in such jurisdiction (except to the extent that any allocation or apportionment method used by such jurisdiction takes into account the income or activities of business entities organized outside the United States of America), taking into account any actual net operating loss carryovers, reduced by

(2) the amount of Income/Capital Taxes which the Indemnatee would be obligated to pay in such jurisdiction (except to the extent that any allocation or apportionment method used by such jurisdiction takes into account the income or activities of business entities organized outside the United States of America), assuming that the transactions contemplated by the Transaction

Documents and Financing Documents had not occurred, taking into account any net operating loss carryovers that would have been available if such transactions or activities had not occurred:

exceeds

(y) any actual aggregate net reduction in Income/Capital Taxes in all other jurisdictions in which the Indemnatee is subject to tax (whether such reduction results from the operation of allocation or apportionment formulas, from credits or otherwise), such aggregate net reduction calculated as:

(1) the aggregate amount of Income/Capital Taxes which the Indemnatee would be obligated to pay in all other jurisdictions in which such Indemnatee is subject to tax, assuming that the transactions contemplated by the Transaction Documents and Financing Documents had not occurred, reduced by

(2) the actual aggregate amount of Income/Capital Taxes which the Indemnatee is obligated to pay in all other jurisdictions in which such Indemnatee is subject to tax;

provided, further, however, that with respect to any tax based on or measured by capital or net worth, the Lessee's indemnity obligation shall not exceed the incremental portion of such Tax attributable to the transactions contemplated by the Transaction Documents;

(iii) Taxes attributable to the Undivided Interest or the Equity Participant's right in the PVNGS Site created by the Real Property Interest that are imposed with respect to any period after the later of (a) the Lease

Termination Date and (b) the date possession of the Undivided Interest has been delivered to the Lessor and the Real Property Interest has been terminated as provided in Section 5(a) of the Facility Lease, unless such Taxes relate to events occurring or matters arising prior to or simultaneously with such date provided that the Lessee shall have fulfilled all of its obligations under the Facility Lease;

(iv) Taxes on or with respect to an Indemnitee arising from any voluntary transfer (it being understood that the term "voluntary transfer" does not include any transfer provided for in the Transaction Documents or the Financing Documents and does not include any transfer to the Lessee or any Affiliate thereof) by such Indemnitee of any interest in the Undivided Interest, the Real Property Interest, the Trust Estate, the Indenture Estate, the Notes or any other right or interest arising under the Transaction Documents or the Financing Documents, unless an Event of Default has occurred and is continuing, or Taxes arising from an involuntary transfer by such Indemnitee of any such interest arising from a bankruptcy or similar proceeding in which such Indemnitee is the debtor unless such bankruptcy or other proceeding relates to the transactions contemplated by the Transaction Documents;

(v) Taxes imposed on an Indemnitee based on or measured by any fees, commission or compensation received by such Indemnitee for acting as trustee, or for other services rendered, in connection with any of the transactions contemplated by the Transaction Documents or the Financing Documents;

(vi) Taxes in the nature of penalties and interest on or with respect to an Indemnitee arising by reason of such Indemnitee's failure to file proper and timely reports or returns (unless the filing of such reports or returns is the obligation of the Lessee under the Transaction Documents or the Financing Documents) imposed by reason of such

Indemnitee's failure to comply with the laws imposing such Tax or its material failure to comply with its obligations under Section 13(b)(6), unless such failure results from any action of the Lessee or failure by the Lessee to comply with any provision of the Transaction Documents or the Financing Documents, including the failure to provide necessary information;

(vii) Taxes on or with respect to an Indemnitee arising as a result of a material failure of such Indemnitee to fulfill its obligations, if any, with respect to the contest of any claim in accordance with Section 13(b)(4) or to provide the Lessee with information reasonably requested by and not otherwise available to the Lessee to enable the Lessee to complete and file or furnish any report, return or statement in accordance with Section 13(b)(5) if such failure effectively precluded the Lessee from effecting a contest of such claim;

(viii) any Taxes imposed on the Lessor resulting from, or which would not have occurred but for, Lessor's Liens, any Taxes imposed on the Equity Participant resulting from, or which would not have occurred but for, Equity Participant's Liens and any Taxes imposed on the Indenture Trustee which would not have occurred but for Indenture Trustee's Liens;

(ix) any Tax on or with respect to any Indemnitee resulting from the gross negligence or willful misconduct of such Indemnitee (it being understood that no Indemnitee is responsible for determining whether a Tax is payable if such Tax is the responsibility of the Lessee under this Section 13(b));

(x) Taxes imposed on or with respect to a transferee (or subsequent transferee) of an original Indemnitee (other than a transferee or subsequent transferee either of which is an Affiliate of the original Indemnitee) to the extent that the amount of such Taxes exceeds the amount of taxes that would have been

imposed on or with respect to such original Indemnatee but for the transfer to such transferee or, if imposed, would not have been subject to indemnification under this Section 13(b); provided, however, that the exception in this clause shall not apply to any transferee where such transfer shall have occurred during the continuance of an Event of Default; and

(xi) any Tax on or with respect to an Indemnatee resulting from any amendment or modification entered into by such Indemnatee to any Transaction Document or Financing Document if the Lessee is not a party to such amendment or modification or has not consented to such amendment or modification, in each case unless an Event of Default shall have occurred and be continuing;

provided, however, that the foregoing paragraphs (i) through (xi) shall not apply to any Tax imposed on the Loan Participant or the indenture estate under the Collateral Trust Indenture.

(3) Calculation of General Tax Indemnity Payments. If any Indemnatee, other than the Equity Participant or any Affiliate thereof or the Trust Estate, realizes a net permanent tax benefit by reason of the payment of any indemnity under Section 13(b)(1), such Indemnatee shall pay the Lessee, but not before the Lessee shall have made all payments theretofore due to such Indemnatee pursuant to this Section 13(b), an amount equal to the lesser of (x) the sum of such tax benefit plus any other net tax benefit realized by such Indemnatee as the result of any payment made by such Indemnatee pursuant to this sentence (determined in a manner consistent with the definition of After-Tax Basis set forth in Appendix A and with the last sentence of Section 13(b)(6)) and (y) the amount of such payment by the Lessee to such Indemnatee and any other payment by the Lessee to such Indemnatee therefore made pursuant to this Section 13(b) less the aggregate amount of all prior payments by such Indemnatee to the Lessee pursuant to this clause (y) with respect to amounts paid pursuant to Section 13(b)(1), it being intended that no such Indemnatee should realize a net tax benefit pursuant

to this Section 13(b) unless the Lessee shall first have been made whole for any payments by it to such Indemnatee pursuant to this Section 13(b); provided, however, that (A) in computing any permanent tax benefit, such Indemnatee shall be deemed first to have utilized all deductions and credits available to it otherwise than by reason of any payment by the Lessee pursuant to this Section 13(b).

(4) General Tax Indemnity-Contests. If a written claim shall be made against any Indemnatee for any Tax for which the Lessee is obligated pursuant to this Section 13(b), such Indemnatee shall notify the Lessee promptly of such claim, but the failure so to notify the Lessee shall not affect any obligation of the Lessee pursuant to this Section 13(b) except as provided in Section 13(b)(2)(vii) (unless the Lessee is otherwise aware of the existence of such claim). If the Lessee shall request in writing within 30 days after receipt of such notice, such Indemnatee shall in good faith and at the Lessee's expense contest the imposition (including the amount) of such Taxes; provided, however, that such Indemnatee may in its sole discretion select the forum for such contest and determine whether any such contest shall be by (A) resisting payment of such Taxes, (B) paying such Taxes under protest or (C) paying such Taxes and seeking a refund thereof; provided further, however, that (X) such Indemnatee shall not be obligated to contest any claim in which the amount in question is less than \$250,000, (Y) at such Indemnatee's option, such contest shall be conducted by the Lessee in the name of such Indemnatee (subject to the preceding proviso) and (Z) in no event shall such Indemnatee be required or the Lessee permitted to contest the imposition of any Taxes for which the Lessee is obligated pursuant to this Section 13(b) unless (v) the Lessee shall have acknowledged its liability to such Indemnatee for an indemnity payment pursuant to this Section 13(b) as a result of such claim if and to the extent such Indemnatee or the Lessee, as the case may be, shall not prevail in the contest of such claim, (w) such Indemnatee shall have received from the Lessee (i) satisfactory indemnity for any liability, expense or loss arising out of or relating to such contest including, but not limited to, (A) all reasonable legal, accountants' and investigatory fees and disbursements, (B) the amount of any

interest, additions to tax or penalty that may be payable as a result of contesting such claim and (C) if such contest is to be initiated by the payment of, and the claiming of a refund for, such Tax, sufficient funds to make such payment on an After-Tax Basis and (ii) an opinion of independent tax counsel selected by the Lessee and approved by such Indemnatee and furnished at the Lessee's sole expense to the effect that a Reasonable Basis exists for contesting such claim or, in the event of an appeal, that there exists a substantial possibility that an appellate court or an administrative agency with appellate jurisdiction, as the case may be, will reverse or substantially modify the adverse determination, (x) the Lessee shall have agreed to pay on demand all reasonable costs and expenses that such Indemnatee may incur in connection with contesting such claim (including, without limitation, all costs, expenses, losses, reasonable legal and accounting fees, disbursements, penalties, interest and additions to tax), (y) such Indemnatee shall have reasonably determined that the action to be taken will not result in any danger of sale, forfeiture or loss of, or the creation of any Lien (except if the Lessee shall have adequately bonded such Lien or otherwise made provision to protect the interests of such Indemnatee in a manner satisfactory to such Indemnatee) on, Unit 2, the Undivided Interest, the Owner Trustee's interest in the PVNGS Site created by the Real Property Interest, or any part of or interest in any of the foregoing, and (z) if such contest shall be conducted in a manner requiring the payment of the claim, the Lessee shall have paid the amount required. The Lessee agrees to give such Indemnatee reasonable notice of any contest prior to the commencement thereof. If any Indemnatee shall obtain a refund of all or any part of any Taxes paid by the Lessee, or if any such refund would be payable to the Indemnatee in the absence of an offsetting liability for Taxes payable to the taxing authority in question (unless such taxing authority would have been foreclosed from asserting such liability but for the contest of such Taxes), such Indemnatee shall pay the Lessee, but not before the Lessee shall have made all payments theretofore due to such Indemnatee pursuant to this Section 13(b), an amount equal to the lesser of (xx) the amount of such refund, including interest received or receivable and attributable thereto or (yy) such tax

payment by the Lessee to such Indemnatee theretofore made pursuant to this Section 13(b), in either case net of any expenses not already paid or incurred by the Lessee; provided, however, that (I) in computing any permanent tax benefit, such Indemnatee shall be deemed first to have utilized all deductions and credits available to it otherwise than by reason of any payment by the Lessee pursuant to this Section 13(b) and (II) notwithstanding the provisions of this Section 13(b)(4), such Indemnatee shall not be obligated to make any payment to the Lessee pursuant to this Section 13(b)(4) if at the time such payment shall be due a Default or an Event of Default shall have occurred and be continuing under the Facility Lease. An Indemnatee shall not be required to make any payment pursuant to this Section 13(b)(4) before such time as the Lessee shall have made all payments and indemnities then due under the Transaction Documents to such Indemnatee. Notwithstanding anything contained in this Section 13(b)(4) to the contrary, no Indemnatee shall be required to contest any claim if the subject matter thereof shall be of a continuing nature and shall have previously been adversely decided pursuant to the contest provisions of this Section 13(b)(4) unless there shall have been a change in the law (including, without limitation, amendments to statutes or regulations, administrative rulings and court decisions) after such claim shall have been so previously decided, and such Indemnatee shall have received an opinion of independent tax counsel selected by the Lessee and approved by such Indemnatee and furnished at the Lessee's sole expense to the effect that such change provides a Reasonable Basis for the position which such Indemnatee and the Lessee, as the case may be, had asserted in such previous contest. Nothing contained in this Section 13(b) shall require any Indemnatee to contest or permit the Lessee to contest a claim which it would otherwise be required to contest pursuant to this Section 13(b) if such Indemnatee shall waive payment by the Lessee of any amount that might otherwise be payable by the Lessee under this Section 13(b) by way of indemnity in respect of such claim.

(5) General Tax Indemnity-Reports. If any report, return or statement is required to be filed with respect to any obligations of the Lessee under or arising out of this Section 13(b), the Lessee

shall timely file the same, except for any such report, return or statement which such Indemnatee has notified the Lessee that it intends to file. The Lessee shall either file such report, return or statement so as to show the ownership of the Undivided Interest in the Owner Trustee and send a copy of such report, return or statement to the Owner Trustee and such Indemnatee or, where not so permitted, notify the Owner Trustee and such Indemnatee of such requirement and prepare and deliver such report, return or statement to the Owner Trustee and such Indemnatee in a manner satisfactory to the Owner Trustee and such Indemnatee within a reasonable time prior to the time such report, return or statement is to be filed or, where such return, statement or report shall be required to reflect items in addition to any obligations of the Lessee under or arising out of this Section 13(b), provide the Owner Trustee and such Indemnatee with information sufficient to permit such return, statement or report to be properly made with respect to any obligations of the Lessee under or arising out of this Section 13(b) (and the Lessee shall hold each Indemnatee harmless from and against any liabilities, obligations, losses, damages, penalties, claims, actions, suits and reasonable costs arising out of any insufficiency or inaccuracy in any such return, statement, report or information). Upon reasonable request by the Lessee, an Indemnatee shall furnish the Lessee with information in the Indemnatee's possession or reasonably obtainable by it (and not otherwise available to the Lessee) necessary for the Lessee to complete any report, return or statement to be filed or furnished by the Lessee. The Lessee shall not have any right to examine the tax returns of any Indemnatee.

(6) General Tax Indemnity-Payment. All Taxes shall be paid when due and payable and, unless otherwise requested by the appropriate Indemnatee, the Lessee shall pay any Taxes for which it is liable pursuant to this Section 13(b) directly to the appropriate taxing authority and shall pay such Indemnatee promptly on demand in immediately available funds any amount due such Indemnatee pursuant to this Section 13(b) with respect to such Taxes. Any such demand shall specify in reasonable detail the payment and the facts upon which the right to payment is based. Each Indemnatee shall promptly

forward to the Lessee any notice, bill or advice received by it concerning any Taxes. Within 30 days after the date of each payment by the Lessee of any Taxes, the Lessee shall furnish the appropriate Indemnatee the original or a certified copy of a receipt for the Lessee's payment of such Taxes or such other evidence of payment of such Taxes as is acceptable to such Indemnatee. The Lessee shall also furnish promptly upon request such data as any Indemnatee may require to enable such Indemnatee to comply with the requirements of any taxing jurisdiction. Whenever any payment is to be made by the Lessee under this Section 13(b) and it shall be necessary, in calculating the After-Tax Basis amount of such payment, to compute the amount of any liability for federal, state or local tax imposed on or measured by the net income of any Indemnatee, such computation shall be based on the assumption that such taxes shall be payable at the highest marginal statutory rate in effect for the relevant period.

(7) Definition of Indemnatee. For purposes of this Section 13(b), the term Indemnatee shall mean and include the successors and assigns of each respective Indemnatee, and for purposes of federal income taxes, the affiliated group of corporations and each member thereof (within the meaning of Section 1504 of the Code) of which such Indemnatee is a member, if such group shall file a consolidated United States federal income tax return, and, for purposes of income or franchise taxes imposed by a particular state or local taxing jurisdiction, shall mean and include any consolidated or combined group of which such Indemnatee is or shall be a member that is treated as such by such state or local taxing jurisdiction.

(c) Supporting Material. Each Indemnatee shall provide to the Lessee such supporting material (other than tax returns) as the Lessee shall reasonably request in connection with the matters set forth in Section 13(b). The Lessee shall reimburse to any Indemnatee any expenses reasonably incurred in providing requested supporting material to the Lessee.

(d) Cooperation. The Equity Participant shall cooperate and shall cause the Owner Trustee to cooperate with and to consider in good faith any reasonable

request by the Lessee upon the written request and at the expense (including a reasonable allowance for internal costs of the Equity Participant) of the Lessee, in order to avoid or minimize any Taxes for which the Lessee is responsible under Section 13(b).

SECTION 14. Transaction Expenses.

(a) Transaction Expenses. Subject to the provisions of paragraph (c) of this Section 14, with funds provided by the Equity Participant, the Owner Trustee hereby agrees that it will pay when due an appropriate portion (taking into account the other undivided interests in Unit 2 being sold on the Closing Date) of the following costs and expenses (Transaction Expenses) without duplication of amounts payable with respect to other undivided interests in Unit 2 sold on the Closing Date:

(i) the reasonable legal fees and disbursements of Morrison & Foerster, Cravath, Swaine & Moore, Morgan, Lewis & Bockius, Shearman & Sterling, Csaplar & Bok, Shaw, Pittman, Potts & Trowbridge, Meyer, Hendricks, Victor, Osborn & Maledon, Davis Polk & Wardwell and White & Case (as counsel for the Indenture Trustee) for their services rendered in connection with the execution and delivery of this Participation Agreement and the other Transaction Documents and all fees, expenses and disbursements incurred by them in connection with such transactions;

(ii) the initial (but not the ongoing) fees and expenses of the Owner Trustee and the Indenture Trustee;

(iii) all stenographic, printing, reproduction, and other reasonable out-of-pocket expenses (other than investment banking or brokerage fees) incurred in connection with the execution and delivery of this Participation Agreement and the other Transaction Documents and all other agreements, documents or instruments prepared in connection therewith (including all computer analysis and travel related costs);

(iv) the fees and expenses of the appraisers for services rendered as contemplated by Section 11(a)(27), the insurance consultant for services rendered as contemplated by Section 11(a)(32), and such other special counsel or consultants as the Equity Participant may require and shall be identified to the Lessee prior to the Closing Date;

(v) all costs of issue of the Bonds issued to refund the Initial Series Notes including, without limitation, the costs of preparing the Financing Documents, all filing fees relating to any Registration Statement and the fees, expenses and disbursements of White & Case, as counsel for the Collateral Trust Trustee, Morrison & Foerster, as counsel for the Agent, and Sullivan & Cromwell, as counsel for the purchasers, or in the event of a public offering of such Bonds, underwriters, of the Bonds, the initial fees of the Collateral Trust Trustee and its out-of-pocket expenses through the applicable Refunding Date, rating agency fees, the fees and commissions of the underwriters of such Bonds and the fees, expenses and disbursements of the Loan Participant; and

(vi) the fees and out-of-pocket expenses of The First Boston Corporation and Lease Management Corporation in connection with the placement of the beneficial interest in the Trust, and the fees referred to in Sections 2(c)(ii) and 2(c)(iii).

Subject to the provisions of paragraph (c) of this Section 14, funds for the payment of Transaction Expenses will be provided by the Equity Participant to the Owner Trustee and the Owner Trustee will promptly disburse such funds.

To the extent not included in Closing Date Transaction Expenses which are disbursed as provided in Section 4(a)(ii), the Owner Trustee shall pay, with funds provided by the Equity Participant, an appropriate portion of Transaction Expenses (other than those referred to in clause (v) above) for which invoices or other requests for payment are received on or prior to November 26, 1986. Such payments shall be disbursed on the first Business Day following the 26th day of each

month, commencing with the month in which the Closing Date occurs, in accordance with payment instructions received from the Lessee. The Lessee shall pay all such Transaction Expenses thereafter; provided, however, that the obligation of the Lessee to pay any such Transaction Expenses shall be discharged, pro tanto, to the extent of any such Transaction Expenses actually paid by the Owner Trustee to the parties entitled thereto.

(b) **Post-Closing Expenses.** The Lessee will pay, on an After-Tax Basis, as Supplemental Rent, (i) the ongoing fees, expenses, disbursements and costs (including legal and other professional fees and expenses) of or incurred by the Owner Trustee, the Indenture Trustee and the Collateral Trust Trustee, including in connection with the issue, sale and purchase of Notes and Bonds after the Closing Date, and (ii) all fees, expenses, disbursements and costs (including legal and other professional fees and expenses including, without limitation, legal and other professional fees and expenses incurred by Agent (including reasonable allocated costs of in-house counsel)) incurred by the Loan Participants, the Equity Participant (including internal costs of the Equity Participant), the Owner Trustee, the Indenture Trustee and the Collateral Trust Trustee in connection with (a) any Default, Event of Default, Indenture Default or Indenture Event of Default, (b) the entering into or giving or withholding of any amendment, modification, supplement, waiver or consent with respect to any Transaction Document or Financing Document, (c) any Event of Loss or Deemed Loss Event, (d) any transfer of all or any part of the right, title and interest of the Indenture Trustee in, to and under the Transaction Documents, (e) any transfer of all or any part of the right, title and interest of the Owner Trustee in the Undivided Interest, the Real Property Interest or in, to and under the Transaction Documents, (f) any transfer contemplated by Section 7(b)(4) and (g) any releveraging, refunding or reoptimization referred to in Section 2(d), 2(e) or 2(f) (except to the extent constituting Transaction Expenses).

(c) **Lessee's Obligation.** Notwithstanding Section 14(a), in the event the transactions contemplated by this Participation Agreement shall not be consummated, the Lessee shall pay or cause to be paid, and shall indemnify and hold harmless the Agent and Original Loan Participants, the Indenture Trustee, the Owner

Trustee and the Equity Participant in respect of all Transaction Expenses other than the fee of Lease Management Corporation referred to in clause (vi) of Section 14(a) unless such failure to consummate shall result solely as a result of a breach by the Equity Participant.

SECTION 15. Equity Participant's Transfers.

(a) Transfers. After the Closing Date (except as provided in Section 7(b)(4)) the Equity Participant shall not assign, convey or otherwise transfer all or any part of (including, without limitation, an undivided interest in) its right, title or interest in and to this Participation Agreement, any of the other Transaction Documents or the Trust Estate (except its right to receive Excepted Payments) to any Person (a Transferee) except on the following conditions:

(i) the Transferee shall enter into an agreement or agreements whereby such Transferee confirms that it shall be bound by the terms of this Participation Agreement and each other Transaction Document, to the extent of the interest transferred, as if it had been originally named as the Equity Participant hereunder and thereunder;

(ii) the Transferee shall be a financial institution, a corporation or a partnership composed of financial institutions or corporations; and

(iii) such transfer shall not violate the Securities Act or any provision of, or create a relationship which would be in violation of, any Applicable Law or agreement to which the transferring Equity Participant or the Transferee is a party or by which its property is bound.

Upon any such transfer that meets all of the foregoing conditions, the transferring Equity Participant shall be released from its obligations under this Participation Agreement and the other Transaction Documents to the extent of the interest transferred. An agreement to transfer shall not in and of itself constitute a transfer for purposes of this Section 15.

(b) Procedure. If the Equity Participant transfers all or any part of its interest hereunder pursuant to this Section 15, it shall give written notice thereof to the Lessee, the Owner Trustee, the Indenture Trustee and the Loan Participants, specifying the name and address for notices to the Transferee, such other information and evidence as shall be necessary to establish compliance with this Section 15 and the extent of the interest transferred to such Transferee. If, as a result of any such transfer, the original Equity Participant is not to continue to receive all payments to be made by the Indenture Trustee to the "Equity Participant" under the Indenture, the original Equity Participant shall from time to time, by notice to the Indenture Trustee, with copies to the Lessee, the Owner Trustee and the Collateral Trust Trustee, designate the manner in which any such payments to the "Equity Participant" are to be allocated, and the Indenture Trustee shall be entitled to rely on such notice for all purposes. This Section 15 shall not apply to the Special Transfer. This Section 15 is for the benefit of the Lessee, the Owner Trustee and the Equity Participant and may not be enforced by any other party hereto.

SECTION 16. Brokerage and Finders' Fees and Commissions.

Except to the extent of amounts payable by the Equity Participant pursuant to Section 14, the Lessee will indemnify and hold harmless the Loan Participants, the Indenture Trustee, the Owner Trustee and the Equity Participant in respect of any commissions, fees, judgments or other expenses of any nature and kind which any of them may become liable to pay by reason of any claims by or on behalf of brokers, finders, agents, advisors or investment bankers in connection with the transactions contemplated by this Participation Agreement, any other Transaction Document, or any litigation or similar proceeding arising from any such claims, other than those claims arising out of written undertakings of the party claiming indemnification under this Section 16 or any Affiliate or shareholder (or Affiliate of such shareholder) of such Person with any such broker, finder, agent, advisor or investment banker.

SECTION 17. Survival of Representations and Warranties; Binding Effect.

(a) **Survival.** All indemnities, representations and warranties contained in this Participation Agreement, in any other Transaction Document, in any Financing Document and in any agreement, document or certificate delivered pursuant hereto or thereto or in connection herewith or therewith, shall survive, and shall continue in effect following, the execution and delivery of this Participation Agreement, the making of the investments and the loans referred to herein, any disposition of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Participation Agreement and the expiration or other termination of any of the Transaction Documents or Financing Documents and shall be and continue in effect notwithstanding (i) any investigation made by the Equity Participant or the Loan Participants or (ii) the fact that any of the Indenture Trustee, the Owner Trustee, the Loan Participants or the Equity Participant may waive compliance with any of the other terms, provisions or conditions of any of the Transaction Documents or Financing Documents. The obligations of the Lessee under Sections 10(b)(1)(vi), 10(b)(1)(vii), 10(b)(2), 10(b)(3)(iv), 10(b)(3)(vii), 10(b)(3)(viii), 10(b)(3)(ix), 10(b)(3)(xi), 10(b)(3)(xiii), 10(b)(3)(xv), 10(b)(3)(xvi), 13, 14, 16 and 19(f) shall survive the expiration or other termination of this Participation Agreement or any other Transaction Document or Financing Document; provided, however, that following the payment in full and cancellation of the Initial Series Notes, the Agent and the Original Loan Participants shall have no further rights under, and the Lessee shall have no further obligations to the Agent and the Original Loan Participants under, Sections 7(b)(4), 10(b)(1)(vi), 10(b)(1)(vii), 10(b)(2), 10(b)(3)(iv), 10(b)(3)(vii), 10(b)(3)(viii), 10(b)(3)(ix), 10(b)(3)(xi), 10(b)(3)(xv), 10(b)(3)(xvi) and 17(b). The modification by law of any statute of limitations or the waiver or extension of any statute of limitations by the Owner Trustee, the Indenture Trustee, the Lessee, the Equity Participant, any Loan Participant or any Indemnatee shall not affect such survival.

(b) **Binding Effect.** All agreements, representations and warranties in this Participation Agreement, the other Transaction Documents and the

Financing Documents and in any agreement, document or certificate delivered concurrently with the execution of this Participation Agreement or from time to time thereafter, shall bind the party making the same and its successors and permitted assigns and shall inure to the benefit of each party for whom made and their respective successors and permitted assigns, and, to the extent provided in the next sentence, each Indemnatee and its successors and assigns. The obligations of the Lessee under Sections 10(b)(3)(viii) and 13 hereof and under Section 20 of the Facility Lease are expressly made for the benefit of, and shall be enforceable by, any Indemnatee, separately or together, without declaring the Facility Lease to be in default and notwithstanding any assignment by the Lessor of the Facility Lease or any of its rights thereunder or any disposition of all or any part of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Participation Agreement, or in this Participation Agreement or any other Transaction Document. All payments required to be made pursuant to Section 10(b)(3)(viii) or 13 shall be made directly to, or as otherwise requested by, the Indemnatee entitled thereto upon written demand by such Indemnatee. Except to the extent permitted by Section 10(b)(3)(ii), the Lessee shall not assign any of its rights or obligations hereunder without the prior written consent of the Equity Participant, the Agent and the Owner Trustee. Except as otherwise indicated, all references herein to any party to this Participation Agreement and the other Transaction Documents shall include the permitted successors and assigns of such party.

SECTION 18. Notices.

All communications, notices and consents provided for herein shall be in writing, and sent by telex, telecopy or other wire transmission containing a request for assurance of receipt in a manner typical with respect to communications of that type, or mailed by registered or certified mail, or personally delivered, and shall be addressed (i) if to the Equity Participant, at Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV; (ii) if to the Agent, at 555 S. Flower Street, Los Angeles, California 90071, Attention: Mr. Gregory House; with a copy to the Agent at Corporate Service Center North, Department No. 1233, 1850 Gateway Blvd., Concord, California 94520, Attention: Ms. Julie

Hopkins (Arizona Public Service Company); (iii) if to Funding Corp, at Corporation Trust Center, 1209 Orange Street, Wilmington Delaware 19801, Attention: President; (iv) if to FNB, or the Owner Trustee, at 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate Trust Division (TWX No. 940581); (v) if to the Indenture Trustee, at 55 Water Street, New York, New York 10041, Attention of Corporate Trust Administration; and (vi) if to the Lessee, at 411 North Central Avenue, P.O. Box 53999, Phoenix, Arizona 85072-3999, Attention: Secretary; or at such other address as any party hereto may from time to time designate by notice duly given in accordance with the provisions of this Section to the other parties hereto. All such communications, notices and consents given in the manner provided above shall be effective on the date of receipt of such communication or notice.

SECTION 19. Miscellaneous.

(a) Execution. This Participation Agreement may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Participation Agreement is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Participation Agreement shall be effective on the latest of such dates.

(b) Intention of the Owner Trustee and the Equity Participant. Each of the Owner Trustee and the Equity Participant intends to exercise its rights and carry out its obligations hereunder and under the other Transaction Documents solely with a view to furthering its own best interests and does not have, and does not expect to have, any form of joint profit motive with any other Person. The Owner Trustee and the Equity Participant shall not be required to share any Rent to which they are entitled under the Facility Lease, or the residual value of the Undivided Interest or the Real Property Interest, with any other Person. The Owner Trustee and the Equity Participant are not under the control of nor shall they be deemed to be under the control of any other Person having any interest in Unit 2, and shall not be the agent of or have a right or

power to bind any such Person (other than the Equity Participant as regards the Owner Trustee) without its express written consent. The Owner Trustee (on behalf of the Equity Participant) and the Equity Participant (on its own behalf) have and at all times shall retain the right separately to take or dispose of the Undivided Interest and the Real Property Interest, subject only to the rights of the Lessee, the Indenture Trustee and the Loan Participants under the Transaction Documents. The Owner Trustee and the Equity Participant accordingly do not intend to create any form of partnership or joint venture with any other Person by virtue of the transactions contemplated hereby or by any of the Transaction Documents. In the event that it is determined, contrary to the intent of the Owner Trustee and the Equity Participant, that, for purposes of the Code or any other income tax law, a form of partnership or joint venture exists between the Owner Trustee or the Equity Participant and any other Person, the Owner Trustee and the Equity Participant hereby elect to the extent permitted by law (i) not to have the partnership provisions of the Code or such other income tax law apply to any of the transactions contemplated hereby or by any of the Transaction Documents and (ii) to be treated solely as owning the Undivided Interest and the Real Property Interest.

(c) **Governing Law.** This Participation Agreement has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York.

(d) **Amendments, Supplements, etc.** Neither this Participation Agreement nor any of the terms hereof may be amended, supplemented, waived or modified orally, but only by an instrument in writing signed by the party against which enforcement of such change is sought.

(e) **Headings.** The headings of the sections and paragraphs of this Participation Agreement have been inserted for convenience of reference only and shall in no way restrict or otherwise modify any of the terms or provisions hereof.

(f) **Bankruptcy of Equity Participant.** If
(a) the Equity Participant or the Owner Trustee becomes a debtor subject to the reorganization provisions of the Bankruptcy Code, or any successor provision,
(b) pursuant to such reorganization provisions the

Equity Participant or the Owner Trustee is required, by reason of the Equity Participant being held to have recourse liability directly or indirectly to the Holder of any Note or the Indenture Trustee, to make payment on account of any amount payable as principal or interest on such Note and (c) such Holder or the Indenture Trustee actually receives any Excess Amount which reflects any payment by the Equity Participant on account of clause (b) of this Section, then such Holder or the Indenture Trustee, as the case may be, shall promptly refund to the Equity Participant such Excess Amount. For purposes of this Section, "Excess Amount" means the amount by which such payment exceeds the amount which would have been received on or prior to the date of such payment by such Holder or the Indenture Trustee if the Equity Participant or the Owner Trustee had not become subject to the recourse liability referred to in clause (b) of this Section. Nothing contained in this Section shall prevent such Holder or the Indenture Trustee from enforcing any personal recourse obligation (and retaining the proceeds thereof) of the Equity Participant expressly provided for under this Participation Agreement.

(g) Entire Agreement. This Participation Agreement, the other Transaction Documents and the Financing Documents supersede all prior agreements, written or oral, between or among any of the parties hereto relating to the transactions contemplated hereby and thereby and each of the parties hereto represents and warrants to the others that this Participation Agreement and the other Transaction Documents and the Financing Documents constitute the entire agreement among the parties relating to the transactions contemplated hereby and thereby.

(h) Publicity. Each party hereto agrees that it will not issue or release for external publication any article or advertising or publicity matter relating to the transactions contemplated hereby or any similar transaction and mentioning or implying the identity of the Equity Participant without the prior written consent of the Equity Participant; provided, however, that the Equity Participant agrees that such consent shall not be withheld if such disclosure is required by Applicable Law.

(i) Capacity of Lessee. In addition to being an ANPP Participant, APS is also the Operating Agent for

PVNGS. The Lessor understands and agrees that APS has certain duties and responsibilities as such Operating Agent under Applicable Law, as well as to the ANPP Participants under the ANPP Project Agreements, and that the obligations of the Lessee hereunder shall not be interpreted as imposing any additional obligation on APS as a result of its status as Operating Agent.

(j) Annex. If and so long as any Initial Series Note shall be and remain Outstanding, the provisions, terms and conditions set forth in Annex A attached hereto shall be and remain in full force and effect and, shall be incorporated into this Participation Agreement, and if any such provisions, terms or condition shall, or shall be construed to, conflict or be inconsistent with any other provision, terms or condition of this Participation Agreement, the former shall prevail and control for all purposes.

(k) Amendment to Appendix. The parties hereto agree to amend the Facility Lease, the Indenture, the Assignment and Assumption and the Deed and Bill of Sale by replacing Appendix A thereto with the form of Appendix A attached hereto.

(l) Lease Amendment. The parties hereto agree to execute an amendment and supplement to the Facility Lease and to file and record such amendment and supplement in all offices in which the Facility Lease was filed or recorded to give effect to the following agreements:

(1) Section 12(b) of the Facility Lease shall be amended to read in its entirety as follows:

(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period not to exceed 2 years (herein referred to as the Fair Market Renewal Term;

and the Fixed Rate Renewal Term (including any extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in which case Basic Rent payable during such Fair Market Renewal Term shall be as set forth in Section 3(a)(iv).

SECTION 20. Section 48(d) Election.

Neither the Equity Participant nor the Owner Trustee makes any representation or warranty to the Lessee or any other Person as to the availability or amount of any investment tax credits with respect to the Undivided Interest, except that the Equity Participant hereby agrees with the Lessee that:

(a) Within 60 days after the execution of this Participation Agreement, the Equity Participant will complete and file with the Lessee a statement in the form of Appendix C hereto (the Section 48(d) Election) executed by the Equity Participant, the Owner Trustee and the common parent (the Common Parent) of the affiliated group of corporations of which the Equity Participant is a member (the Group);

(b) The Equity Participant will attach and will cause the Common Parent and direct the Owner Trustee to attach to their respective Federal income tax returns and to the consolidated Federal income tax return of the Group for their respective taxable years in which the Facility Lease commences a summary statement in the form of Appendix D hereto (the Summary Statement);

(c) The Equity Participant will keep and will cause the Common Parent and direct the Owner Trustee to keep the Section 48(d) Election as part of their respective records; and

(d) The Equity Participant will not transfer its interest in the Trust Estate, and will not cause the Owner Trustee to transfer the Undivided Interest, at any time during the Lease Term when a loss or recapture of investment tax credits would occur, to a Person whose status as lessor of the Undivided Interest would result in the loss or recapture of any investment tax credits claimed by the Lessee with respect to the Undivided Interest; provided, however, that if the Equity Participant gives the Lessee notice of a proposed

transfer and the Lessee fails to object to the transfer on such grounds within 30 days of such notice, then the completion of such proposed transfer will not be considered a violation of this covenant.

IN WITNESS WHEREOF, the parties hereto have each caused this Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By _____
Senior Vice President

Date: August 18, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Banks

By: _____

Title: _____

By: _____
Gregory House
Assistant Vice President

Date: August 18, 1986

PVNGS FUNDING CORP., INC.

By _____
Vice President

Date: August 18, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Vice President and Treasurer

Date: August 18, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner
Trustee

By: _____
Assistant Vice President

Date: August 18, 1986

CHEMICAL BANK, in its indi-
vidual capacity and as
Indenture Trustee

By _____
Vice President

Date: August 18, 1986

Schedule 1

ARIZONA PUBLIC SERVICE COMPANY
PALO VERDE NUCLEAR GENERATING
STATION UNIT 2

<u>BANK</u>	<u>LOAN PERCENTAGE</u>
Bank of America National Trust and Savings Association	10.526315730
Mellon Bank, N.A.	7.368421055
The Chase Manhattan Bank, N.A.	6.315789480
Chemical Bank	6.315789480
Citibank, N.A.	6.315789480
Continental Illinois National Bank and Trust Company	6.315789480
First Interstate Bank of California	6.315789480
Marine Midland Bank, N.A.	6.315789480
The Bank of New York	4.210526321
Irving Trust Company	4.210526321
Wells Fargo Bank	4.210526321
The Arizona Bank	2.105263158
Credit Suisse	2.105263158
The First National Bank of Boston	2.105263158
NCNB National Bank of North Carolina	2.105263158
United Bank of Arizona	2.105263158
The Valley National Bank of Arizona	1.052631582

Schedule 2

ARIZONA PUBLIC SERVICE COMPANY

PALO VERDE NUCLEAR GENERATING
STATION UNIT 2

NOTICE OF CLOSING

SECURITY PACIFIC CAPITAL LEASING CORPORATION

Pursuant to Section 5(a) of the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among Security Pacific Capital Leasing Corporation, as Equity Participant, Bank of America, National Trust and Savings Association, for itself and as agent for the Banks referred to in Schedule 1 of the Participation Agreement, PVNGS Funding Corp., Inc., The First National Bank of Boston, as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, and Arizona Public Service Company, as Lessee, Arizona Public Service Company hereby gives notice of a Closing to occur at 10:00 a.m. on August 18, 1986 (the Closing Date). The Closing will be held at the offices of Mudge Rose Guthrie Alexander & Ferdon, 180 Maiden Lane, New York, New York 10038.

(i) Purchase Price is \$

(ii) Real Estate Investment is
\$

(iii) The maximum aggregate amount of the
Loans is \$

(iv) Based upon information supplied to Arizona Public Service Company, Closing Date Transaction Expenses are an aggregate of [\$]. Instructions with respect to such Closing Date Transaction Expenses are attached hereto.

(v) Payment of the Purchase Price, the Real Estate Investment and the Closing Date Transaction Expenses shall be made pursuant to the Omnibus Transfer Instruction and Receipt dated August __, 1986 (a copy of which is attached hereto).

Capitalized terms used herein and not otherwise specifically defined herein shall have the meanings set forth in Appendix A to the Participation Agreement.

IN WITNESS WHEREOF, Arizona Public Service Company has executed this Notice of Closing this 18th day of August, 1986.

ARIZONA PUBLIC SERVICE
COMPANY

By Paul A. Williams II

Schedule 3

EQUITY PARTICIPANT INFORMATION; PRICING ASSUMPTIONS

Basic Rent, Casualty Values, Special Casualty Values, Modified Special Casualty Values and Extraordinary Casualty Values, as set forth in the Facility Lease as originally executed, have been computed on the basis of the following pricing assumptions:

1. Investment Percentage: 20.00%
2. Loan Percentage: 80.00%
3. Interest Rate on Notes: 8% per annum through December 31, 1986 and 10.15% per annum thereafter.
4. Federal ACRS Deductions: 10-year public utility property deductions based on the Purchase Price.
5. Equity Participant's Tax Year-End: December 31, 1986.
6. Closing Date: August 18, 1986.
7. Transaction Expenses: 0.75% of Facility Cost paid by the Equity Participant in addition to its Investment (amortized on a straight-line basis during the Basic Lease Term).
8. Real Estate Investment: .05% of Facility Cost.
9. Basic Rent Payment Date: June 30 and December 30 of each year (rent payable in arrears).

10. First Basic Rent Payment Date:	June 30, 1987.
11. Last Basic Rent Payment Date:	December 30, 2015.
12. Interim Rent Payment Date:	December 30, 1986.
13. Rent Structure	Semi-Annual Arrears
14. Equity Participant's Tax Rates	Federal-46%; State-8.75%
15. First Estimated Tax Payment Date:	October 15, 1986.
16. Tax Accounting Method:	Accrual.
17. Amortization of Notes:	See schedule 4 attached hereto.
18. Lessor's Portion:	12.6993%
19. Unit 2 Interest:	3.6955%
20. Unit 2 Retained Assets Portion:	13.1250%
21. Facility Cost:	\$141,250,000
22. Purchase Price:	99.95% of Facility Cost

Schedule 4

Amortization of Initial Series Note

Date	Principal
12/30/1986	0.0000000
6/30/1987	0.1791784
12/30/1987	0.1882717
6/30/1988	0.1978265
12/30/1988	0.2078661
6/30/1989	0.2184154
12/30/1989	0.2294999
6/30/1990	0.2411471
12/30/1990	0.2533853
6/30/1991	0.2662446
12/30/1991	0.2797565
6/30/1992	0.2939541
12/30/1992	0.3088723
6/30/1993	0.3245476
12/30/1993	0.3410184
6/30/1994	0.3583250
12/30/1994	0.3765100
6/30/1995	0.3956179
12/30/1995	0.4156955
6/30/1996	0.4367921
12/30/1996	0.4589593
6/30/1997	0.4822515
12/30/1997	1.6743209
6/30/1998	1.7592927
12/30/1998	1.8485768
6/30/1999	1.9423921
12/30/1999	2.0409685
6/30/2000	2.1445476
12/30/2000	2.2533834
6/30/2001	2.3677426
12/30/2001	2.4879056
6/30/2002	2.6141667
12/30/2002	2.7468357
6/30/2003	2.8862376
12/30/2003	3.0327142
6/30/2004	3.1866245
12/30/2004	3.3483456
6/30/2005	3.5182742
12/30/2005	3.6968266
6/30/2006	3.8844405
12/30/2006	4.0815759
6/30/2007	4.2887159
12/30/2007	4.5063682
6/30/2008	4.7350664

Date	Principal
12/30/2008	4.9753710
6/30/2009	5.2278711
12/30/2009	5.4931855
6/30/2010	5.7719647
12/30/2010	6.0648920
6/30/2011	0.9672583
12/30/2011	0.0000000
6/30/2012	0.0000000
12/30/2012	0.0000000
6/30/2013	0.0000000
12/30/2013	0.0000000
6/30/2014	0.0000000
12/30/2014	0.0000000
6/30/2015	0.0000000
12/30/2015	0.0000000

Schedule 5

Recordations and Filings

Part I. Recordations in Respect of the Sale of, and the Owner Trustee's Title to, the Undivided Interest and the Real Property Interest.

County Recorder, Maricopa County, Arizona:

- (i) Deed;
- (ii) Bill of Sale;
- (iii) Assignment and Assumption;
- (iv) Facility Lease;
- (v) Indenture;
- (vi) Mortgage Release; and
- (vii) Affidavit of Real Property Value.

Part II. UCC-1 Financing Statements.

A. County Recorder, Maricopa County, Arizona:

(i) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease; and

(ii) A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

B. Secretary of State, Arizona:

(i) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease;

(ii) A financing statement on form UCC-1 naming APS, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, in respect of the Facility Lease to be filed as a public utility; and

(iii) A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

C. Massachusetts/state and local:

A financing statement on form UCC-1 naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate.

Part III. Other Filings.

A. County Recorder, Maricopa County, Arizona:

A partial release on form UCC-2 naming APS, as debtor, and Security Pacific National Bank, as Secured Party.

B. Secretary of State, Arizona:

A partial release on form UCC-2 naming APS, as debtor, and Security Pacific National Bank, as Secured Party.

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof", "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the initial series of Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Aggregate Liability shall mean the amount of Aggregate Liability for a single Nuclear Incident of all Persons Indemnified, as determined in accordance with the Price-Anderson Act.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Adjustment Factor shall mean the quotient obtained by dividing the number of Nuclear Facilities having operating licenses by 100.

Affiliate, with respect to any Person, shall mean any other Person directly

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Adjustment Factor shall mean the quotient obtained by dividing the number of Nuclear Facilities having operating licenses by 100.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive) or accrual of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

Aggregate Liability shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "aggregate liability", the term "Aggregate Liability" shall be similarly expanded.

ANPP

Aggregate Liability shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "aggregate liability", the term "Aggregate Liability" shall be similarly expanded.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 13(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes, as amended.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated as of August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under the Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York, Boston, Massachusetts or San Francisco, California are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement is or is not included or reflected in the plans and specifications for Unit 2, as

built, and (b) any alteration, modification, addition or improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation), of any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean a Collateral Trust Indenture among APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS facilities which are common to all generating units, including Unit 2, at PVNGS.

Common Parent shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien

existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Expert shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deed shall mean the Deed, dated as of August 18, 1986, from APS to the Owner Trustee.

Deemed Loss Event shall mean any of the following events (unless and until waived in writing by the Equity Participant):

(1) Utility Regulation. If at any time from and including the Closing Date and before the Lease Termination Date, the Lessor or the Equity Participant, by reason of the acquisition or ownership of the Undivided Interest or the Real Property Interest or any part thereof by the Lessor (or any beneficial interest therein by the Equity Participant) or the lease of the Undivided Interest to the Lessee or any of the other transactions contemplated by the Transaction Documents, shall be deemed by any Governmental Authority having jurisdiction to be, or shall become subject to regulation (other than Non-Burdensome Regulation) as, an electric utility, a public utility or a holding company under any Applicable Law or as a consequence of any Governmental Action, and the effect thereof on the Lessor or the Equity Participant would be, in the sole judgment of the Equity Participant, acting on the advice of counsel, adverse, except that if the Lessee, at its sole cost and expense, is contesting diligently and in good faith any Governmental Action which would otherwise constitute a Deemed Loss Event under this clause (1), such Deemed Loss Event shall be deemed not to have occurred so long as in the sole judgment of the Equity Participant (i) such contest does not involve any danger of the foreclosure, sale, forfeiture or loss of, or the creation of any Lien on, the Undivided Interest, the Real Property Interest or any part thereof or any interest therein, (ii) such contest does not adversely affect the Undivided Interest or the Real Property Interest or any part thereof or any other property, assets or rights of the Lessor or the Equity Participant or the lien of the Indenture thereon, (iii) the Lessee shall have furnished the Equity Participant with an opinion of independent counsel satisfactory to the Equity Participant to the effect that (a) there exists a reasonable basis for contesting such determination or (b) in the case of any action arising from or related to the Lessor or the Equity Participant under the Holding Company Act, it is more likely than not that the Lessee will

successfully contest such determination without the need for any appeal, (iv) such determination shall be effectively stayed or withdrawn during such contest (and shall not in the sole judgment of the Equity Participant be subject to retroactive application at the conclusion of such contest) in a manner satisfactory to the Equity Participant, and the Equity Participant shall have determined in its sole judgment that such contest and the Lessor's continued ownership of the Undivided Interest and the Real Property Interest during the pendency of such contest will not adversely affect its business or the business of any of its Affiliates, and (v) the Lessee shall have indemnified the Lessor and the Equity Participant in a manner satisfactory to the Equity Participant for any liability or loss which either may incur; it being understood, however, that the term Equity Participant as used in this clause (1) does not include any Transferee who at the time of transfer is an entity which is subject to regulation as an electric utility, public utility or a holding company under Applicable Law or Governmental Action.

(2) Change in Applicable Law. Any change in, or new interpretation by a Governmental Authority having jurisdiction relating to, Applicable Law, including, without limitation, the Price-Anderson Act, the Atomic Energy Act, the Nuclear Waste Act or the regulations of the NRC, in each case as in effect on the Closing Date; as a result of which, in the opinion of independent counsel to the Equity Participant: (i) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified is increased; (ii) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified exceeds the amount of Financial Protection required under Applicable Law and available at the time of such Nuclear Incident; (iii) (a) the amount of Primary Financial Protection required with respect to a single Nuclear Facility under Applicable Law is increased, whether or not the total amount of Financial Protection required with respect to a single Nuclear Facility is increased, or (b) the amount of Financial Protection required under Applicable Law is increased (including, but not limited to, an increase in the amount of retrospective premiums payable under the Retrospective Rating Plan) or (c) the amount of

retrospective premiums payable under the Retrospective Rating Plan in any one year with respect to two or more Nuclear Incidents is increased; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. Section 140.22 or 10 C.F.R. Section 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan) shall be modified or changed in any material respect; (v) the Lessor or the Equity Participant may become liable or responsible in any capacity (including, without limitation, through assessments imposed by a Governmental Authority) for payments owed in respect of the Nuclear Waste Fund (as such term is used in Section 302 of the Nuclear Waste Act) or in respect of the handling or disposal of nuclear waste, decontamination, storage, transportation or safekeeping of radioactive or hazardous materials or any other obligation in the nature of the foregoing; (vi) the Lessor, the Equity Participant or the Lessee may be prohibited from asserting any right, protection or defense available under Applicable Law as of the Closing Date with respect to civil or criminal actions brought in connection with a Nuclear Incident (including, without limitation, through an expansion of the waiver of defenses provision under subsection 170n. of the Atomic Energy Act); (vii) there shall be expressly created a new cause of action whereby any Person who pays or will pay retrospective premiums under the Retrospective Rating Plan or other assessments required under Applicable Law may recover the amount of such payments from the facility at which a Nuclear Incident occurs or from any Person associated with such facility; (viii) there shall be a third tier or additional level of potential or real liability (including assessments imposed by a Governmental Authority) with respect to a Nuclear Facility; (ix) there shall be any type of claim, liability or expense (other than the costs of investigating and settling claims and defending suits for damage) excluded from the limitation of liability established by the Price-Anderson Act (through modification of the definitions of "aggregate liability", "persons indemnified", "nuclear incident" or otherwise) or excluded (or the funding or payment thereof deferred) under insurance or other Financial Protection required under Applicable Law as in effect on the Closing Date, except to the

extent and in the amount expressly excluded or deferred pursuant to Applicable Law as in effect on the Closing Date; or (x) the Lessor or the Equity Participant may be exposed, during the Lease Term or after the Lease Termination Date, to any other increased real or potential liability (including, without limitation, through assessments imposed by a Governmental Authority) with respect to a Nuclear Incident or otherwise relating to the operation of PVNGS or the transactions contemplated by the Participation Agreement; provided, however, that no such change shall constitute a Deemed Loss Event if and for so long as such change or interpretation meets all the conditions constituting a Safe Harbor Change. For purposes of this clause (2), the requirement or existence of insurance, retrospective premiums, indemnities (whether by the Lessee or any other Person) or other forms of Financial Protection (similar or dissimilar to the foregoing) shall not be deemed to eliminate or negate any exposure of the Lessor or the Equity Participant to real or potential increased liability.

(3) Insurance. The Lessee shall not be in compliance with Section 10 of the Facility Lease.

(4) License. Any expiration, revocation, suspension, amendment or interpretation by any Governmental Authority of the License or any other change in Applicable Law or Governmental Action, as a result of which, prior to the Lease Termination Date, either the Lessor or the Equity Participant is or might (i) be required to be or become a licensee under the Atomic Energy Act with respect to Unit 2 or (ii) be subject to the obligations or liabilities imposed, as of the Closing Date or thereafter, on licensees under the Atomic Energy Act with respect to Unit 2 or (iii) be otherwise subject to significant regulation.

(5) Multiple Incidents. The occurrence (i) of two or more incidents (including incidents occurring outside the United States of America), in each case at any Nuclear Facility or Facilities using a Combustion Engineering pressurized water reactor nuclear steam supply system or another nuclear steam supply system of comparable design or comparable components, the failure of which Combustion Engineering pressurized water reactor nuclear steam

supply system or other nuclear steam supply system of comparable design or components results in (x) a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; (y) (A) the radiation level in the containment vessel as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equaling or exceeding 1,000 rad per hour; or (B) any measure of radioactivity in the primary coolant system exceeding by 1,000 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (z) damage to offsite property, including, without limitation, costs for decontamination, in amounts in excess of \$15,000,000; or (ii) within a five-year period of three or more incidents, of the type and severity described in subclause (i)(x), (y) or (z) above, at any Nuclear Facility or Facilities (including incidents occurring outside the United States of America).

(6) **Illegality; Exercise of Rights and Remedies.** Any change in Applicable Law or any Governmental Action the effect of which is or might be (i) to make any of the transactions contemplated by the Transaction Documents unauthorized, illegal,

or otherwise contrary to Applicable Law, (ii) to impede the exercise by the Lessor or the Equity Participant of any right or remedy under any Transaction Document relating to the assertion of claims for Rent or monetary damages, (iii) to cause the Lessor or the Equity Participant to be or become liable in any capacity in respect of Decommissioning, including, without limitation, all or any portion of the Termination Obligation (as defined in the ANPP Participation Agreement), or (iv) to constitute an assertion to the effect that (a) the exercise by the Lessor or the Equity Participant of any right (irrespective of the event giving rise to such right) under any Transaction Document would constitute impermissible control over Unit 2 or the licensees of Unit 2, other than an assertion consistent with the second sentence of Section 184 of the Atomic Energy Act and the NRC's regulations thereunder, including, without limitation, 10 C.F.R. Section 50.81, as now in effect, or (b) the acquisition or transfer of the Undivided Interest was in violation of, or otherwise contrary to, Applicable Law.

(7) Violations. With respect to PVNGS, the NRC shall have issued within a two-year period (x) two or more final orders involving "Severity Level I" violations or (y) three or more final orders involving "Severity Level I" or "Severity Level II" violations, as such terms are used in Supplement I to Appendix C to 10 C.F.R., Part 2, as in effect on the Closing Date (or, if such Supplement is amended or superseded or different categories are in effect, comparable violations).

(8) Unit 1 and Unit 3 Incidents. (1) The occurrence of an event at Unit 1 or Unit 3 (such affected unit being herein in this definition referred to as the Affected Unit) as a result of which: (w) the radiation level in the top half of the containment vessel of the Affected Unit as measured by the average of two high range radiation monitors in the upper half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of the Affected Unit shall exceed by 100 times the limiting conditions for operation specified in the

technical specifications for the Affected Unit (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of the Affected Unit's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of the Affected Unit, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date; or (2) the occurrence of a Nuclear Incident at an Affected Unit as a result of which the Affected Unit ceases to operate (or if the Affected Unit is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 36 consecutive months.

(9) Radiation Level. Except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 1 or 3, the radiation level in the fuel building above either such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours.

(10) Reduced Operations. Other than in consequence of a reduction in demand, Unit 2 shall have operated in any calendar year at a net capacity factor below 35% other than as a result of a

shutdown to repair damage to Unit 2; provided, however, that if the NRC shall determine at any time during the Lease Term that the operation of this paragraph might impair the ability of the Lessee or the Operating Agent to comply with the terms of the License or Applicable Law or interfere with the exercise of the NRC's jurisdiction to protect the public health and safety, then this paragraph 10 shall be deemed waived.

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank (as used herein, a Letter of Credit Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Letter of Credit Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Letter of Credit Bank, or (iii) any Letter of Credit Bank whose long-term unsecured debt securities are rated not less than Aa3 by Moody's, other than a Letter of Credit Bank to which the Equity Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of a Letter of Credit Bank which is part of a holding company structure, the failure of such Letter of Credit Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities); provided, however, that any Letter of Credit issued by a Letter of Credit Bank that is not incorporated in the United States shall provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Security Pacific Capital Leasing Corporation, and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended.

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean (i) all indemnity payments to which the Owner Trustee or the Equity Participant (or the respective successors, assigns; agents, officers, directors or employees of the Owner Trustee or the Equity Participant) is entitled, (ii) any amounts payable under any Transaction Document to reimburse the Lessor or the Equity Participant (including the reasonable expenses of the Lessor or the Equity Participant incurred in connection with any such payment) for performing or complying with any of the obligations of the Lessee under and as permitted by any Transaction Document, (iii) any insurance proceeds with respect to an Event of Loss in excess of amounts then due and owing in respect of the principal of and premium, if any, and interest on all Notes Outstanding, (iv) any insurance proceeds (or payments with respect to risks self-insured) under liability policies, (v) any payments in respect of interest to the extent attributable to payments referred to in clauses (i) through (iv) above and (vi) if the Letter of Credit has been terminated or has expired, a portion of Casualty Value, Special Casualty Value or Extraordinary Casualty Value equal to the amount by which Modified Special Casualty Value exceeds the sum of all amounts drawn under the Letter of Credit.

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and all rights and interests with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank.

Extraordinary Casualty Value, as of any date, during the Basic Lease Term, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under the applicable provision, if any, of the Facility Lease or the Participation Agreement, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Extraordinary Nuclear Occurrence shall have the meaning assigned in Section 11 of the Atomic Energy Act and the related NRC regulations (10 C.F.R. § 140.84 and 140.85), as in effect as of the Closing Date.

Facility Cost shall mean the sum of the Purchase Price and the Real Estate Investment plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement; and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended.

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; (y) any order or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period exceeding 24 months; or (z) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which: (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-92Z47 (as in effect on the Closing Date), using independent assessments based on any one of

the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which: (x) the NRC declares to be an Extraordinary Nuclear Occurrence; (y) result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; or (z) result in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and

over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee, or of the Lessee and one or more other ANPP Participants, to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown in consequence of the occurrence of an event described in (A) clause (4) or (5) above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause (8) above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months.

Financial Protection shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "financial protection", the term "Financial Protection" shall be similarly expanded.

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meaning set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, shall mean the Generation Entitlement Share of APS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all siting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Group shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, each Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture, and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles, a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean that portion of APS's interest in Unit 2 equal to the percentage set forth on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended,

(vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Aggregate Loss shall be computed and applied in respect of Unit 2, including all interests therein, and with respect to each calendar year shall mean the sum of (i) retrospective premiums, if any, payable during such year under the Retrospective Rating Plan with respect to any Nuclear Incident which shall have occurred prior to the date of such calculation, (ii) all uninsured liquidated amounts paid or payable during such year, and not covered by the Retrospective Rating Plan, in respect of Nuclear Incidents, and (iii) other known assessments and costs and an assumed additional amount in respect of such retrospective premiums which would be payable during such year if a Nuclear Incident, or one additional Nuclear Incident, should occur in such year.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of (x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of the Fixed Rate Renewal Term) in each

case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets Portion of the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and (iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets Portion of the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or December 31 in such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage.

-Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions. The after-tax yield component of Net Economic Return will be adjusted upward by 0.1% for each 1% downward adjustment in marginal federal tax rates pursuant to a Change in Tax Law; provided, however, that the maximum upward adjustment due solely to such increase in the after-tax yield component will result in an increase of .20% in the present value of Rent (discounted semi-annually using a semi-annual discount rate equal to 5.075%).

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Net Worth Factor shall mean the quotient obtained by dividing (i) PVNGS Net Worth, as of December 31 of the year prior to the date of any calculation of Net Worth Factor, by (ii) PVNGS Net Worth, as of December 31, 1985; provided, however, that Net Worth Factor shall not be less than 1.0 in respect of any year prior to 1991.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest and the Real Property Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest and the Real Property Interest on or after the Lease Termination Date or (iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes and Additional Notes issued from time to time under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Facility shall mean a facility designed for producing substantial amounts of electricity and having a rated capacity of 100,000 electrical kilowatts or more.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act, as in effect as of the Closing Date; provided that if the Atomic Energy Act shall be amended to expand the definition of "nuclear incident", the term "Nuclear Incident" shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used or by a Contract Administrator.

Original Loan Participants shall mean Bank of America and each of the other banks (the Banks) listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% per annum in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs), or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participants and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been

made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest) under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

Persons Indemnified shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "person indemnified", the term "Persons Indemnified" shall be similarly expanded.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No: 85-256, 71 Stat. 576 (1957); as amended to August 18, 1986 (except as otherwise expressly provided), including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 3 to the Participation Agreement.

Primary Financial Protection shall mean Financial Protection required to be maintained by each Nuclear Facility under Applicable Law, except for such amounts required to be maintained under a Retrospective Rating Plan.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Net Worth shall mean the sum of the consolidated common stockholders equity of APS, El Paso, PNM and Southern California, and their respective successors, as shown in their most recent respective audited financial statements; provided, however, that the consolidated common stockholders equity of any such Person shall not be included in the foregoing sum after (and only after) such time as such Person is not an ANPP Participant subject to the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 4(b) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed or by the ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund the Initial Series Notes or Outstanding Bonds.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean a Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of Refunding Bonds.

Registration Statement shall mean a registration statement, including all exhibits and all documents incorporated in such Registration Statement by reference, filed with the SEC under the Securities Act in connection with the offer, issue and sale of any Refunding Bonds or Refunding Notes.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent.

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Severable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Retrospective Rating Plan shall mean the industry retrospective rating plan established pursuant to the Price-Anderson Act, or any successor or similar plan established under Applicable Law.

Safe Harbor Change shall mean any Substantial Amendment, and any other change which, had it been part of the first Substantial Amendment (together with all other changes since the first Substantial Amendment) would have been a Substantial Amendment, enacted after

the Closing Date, if, upon the effective date of such Substantial Amendment or other change and at all times thereafter (as shall be determined from time to time):

(A) (1) the Lessor and the Equity Participant (x) shall, as a result of such Substantial Amendment, be exempt from all real and potential liability in respect of a Nuclear Incident (Nuclear Liability) both during and after the Lease Term (unless the Equity Participant or the Lessor, as the case may be, is as of the time of a Nuclear Incident a licensee with respect to Unit 2 under the Atomic Energy Act) and (y) shall have received an opinion of independent counsel to the Equity Participant to the effect that there is no reasonable basis for a court to hold either the Lessor or the Equity Participant liable for any Nuclear Liability, both during and after the Lease Term (subject to the exception described in the parenthetical clause in clause (x) above) and (2) in the opinion of independent counsel to the Equity Participant, such Substantial Amendment meets all the conditions stated in clause (B) below; provided, however, that part (b) in subclause (i) of clause (B) shall read as follows, "(b) the product of (1) 1.75 times (2) the Net Worth Factor times (3) the product of \$6.5 billion multiplied by the Adjustment Factor***", and subclause (iii) of clause (B) shall read as follows, "Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter shall not exceed the product of (x) 1.75 times (y) .5% times (z) the product of the Net Worth Factor times \$6.5 billion ***"; provided, further, that in the event the Equity Participant is furnished with an opinion of its independent counsel stating that, because of a change in Applicable Law, there is a significant risk that the opinion described in subclause (y) of subclause (1) above is no longer valid, then this clause (A) shall cease to be applicable; or

(B) in the event clause (A) is not applicable, as a result of such Substantial Amendment, in the opinion of independent counsel to the Equity Participant: (i) Adjusted Aggregate Liability, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed (a) the amount of Financial Protection required to be maintained by each Nuclear Facility with respect to a single Nuclear Incident or (b) the product of (1) the Net Worth Factor times (2) the product of \$6.5 billion times (3) the Adjustment Factor, and if Adjusted Aggregate Liability should exceed either (a) or (b) above the Substantial Amendment shall no longer constitute a Safe Harbor Change; (ii) the amount of Primary Financial Protection available from commercial insurance underwriters on terms substantially equivalent (in the reasonable opinion of the Equity Participant) to the terms in effect on the Closing Date under Applicable Law and required to be maintained by licensees with respect to any single Nuclear Facility shall be at least equal to the amount required under Applicable Law (which amount shall not exceed \$500 million); (iii) Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed the product of (x) .5% times (y) the Net Worth Factor times (z) \$6.5 billion, and if Maximum Aggregate Loss should exceed the foregoing product the Substantial Amendment shall no longer constitute a Safe Harbor Change; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. § 140.22, or 10 C.F.R. § 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan), as in effect on the Closing Date, shall not have been amended or modified in any material respect; (v) the NRC shall be required to fulfill payment obligations when due from

a. licensee liable for damage arising out of or related to a Nuclear Incident in the event that the payment obligations of such licensee in any calendar year exceed the amount payable by such licensee in respect of such Nuclear Facility in such year under the Retrospective Rating Plan; provided, however, that the NRC shall be entitled to reimbursement through the Retrospective Rating Plan as such payments are made over time; (vi) neither the Lessee nor any other Persons Indemnified will be required to waive the defense of the statute of limitations (existing under any Applicable Law) with respect to a Nuclear Incident (except an Extraordinary Nuclear Occurrence); with respect to an Extraordinary Nuclear Occurrence such defense shall be required to be waived only as to suits instituted within 30 years after the date the Extraordinary Nuclear Occurrence which is the subject of the suit takes place and within a prescribed number of years from the date on which the claimant first knew, or reasonably could have known, of his injury or damage and the cause thereof; (vii) neither the Lessor nor the Equity Participant shall be exposed to any increased real or potential liability (including assessments imposed by a Governmental Authority) with respect to activities authorized by the Nuclear Waste Act; (viii) none of the results contemplated in subclauses (vii) and (ix) of clause (2) of the definition of Deemed Loss Event shall have occurred; (ix) neither the Lessor nor the Equity Participant shall, in the opinion of independent counsel to the Equity Participant delivered within six months of such Substantial Amendment, be exposed to any other material increase in its real or potential liability with respect to a Nuclear Incident, either before, on or after the Lease Termination Date, except for liability arising with respect to a Nuclear Incident which takes place after the Lessor or the Equity

Participant, as the case may, becomes a licensee of the NRC, and (x) neither the Lessor, the Equity Participant nor the Lessee shall be prohibited from asserting any other right, protection or defense available under Applicable Law as in effect on the Closing Date other than those rights, protections and defenses which are waived pursuant to this definition of Safe Harbor Change; provided, however, that an expansion of the waiver of defenses provision of subsection 170n.(1) of the Atomic Energy Act so that such waivers are applicable with respect to an Extraordinary Nuclear Occurrence arising out of or resulting from or occurring in the course of (a) transportation of source material, byproduct material, or special nuclear material to or from any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, (b) activities undertaken by the Secretary, including but not limited to activities related to the storage or disposal of high-level radioactive waste, or (c) the construction, possession or operation of any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, shall not be deemed to expose the Lessor, the Equity Participant or the Lessee to any increased real or potential liability.

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor, the Equity Participant and the Indenture Trustee in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Secretary shall mean the Secretary of Energy.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining a residual of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding,

Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted securities ratings.

Summary Statement shall have the meaning set forth in Section 20(b) of the Participation Agreement.

Substantial Amendment shall mean any amendment to the Price-Anderson Act or the Atomic Energy Act which would constitute a Deemed Loss Event under clause (2) of the definition of Deemed Loss Event.

Substituted Lessee shall have the meaning set forth in Section 6.8(c) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Equity Participant.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property (personal or real, tangible or intangible) and stamp taxes), levies, imposts, duties, charges, assessments or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon.

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed (or ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement) by an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Security Pacific Capital Leasing Corporation and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease

Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp, APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale; (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data-links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common facilities); (xiii) simulator; and (xiv) oil and diesel fuel-inventories; (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements; and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii) railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

Appendix B
to
Participation Agreement

BILL OF SALE AND ASSIGNMENT

BILL OF SALE AND ASSIGNMENT

dated as of _____, 19__

from

[SECURITY PACIFIC CAPITAL LEASING CORPORATION]

to

ARIZONA PUBLIC SERVICE COMPANY

BILL OF SALE AND ASSIGNMENT, dated as of _____, 19____, from SECURITY PACIFIC CAPITAL LEASING CORPORATION a [Delaware] corporation (the Equity Participant), to ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (APS).

W I T N E S S E T H:

WHEREAS, pursuant to Section 7(b)(4) of the Participation Agreement dated as of August 1, 1986 among the Equity Participant, PVNGS Funding Corp., Inc., Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants, The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee and APS, as Lessee (the Participation Agreement), the Equity Participant desires to sell and APS desires to buy the Assigned Property (as hereinafter defined);

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.01. Definitions. For purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in the Participation Agreement.

ARTICLE II

ASSIGNMENT OF TRUST ESTATE

SECTION 2.01. Assignment. Equity Participant does hereby grant, bargain, convey, sell, assign, transfer and set over to APS, on an as is, where is basis, free and clear of Equity Participant's Liens but otherwise without recourse, representation or warranty, express or implied, of any nature whatsoever, all Equity Participant's right, title and interest in, to and under the Trust Estate except Excepted Rights and the Equity Participant's right to receive Excepted Payments (the Assigned Property) [, subject to Equity Participant's

security interest in, and general lien upon, all the right, title, and interest of APS, as successor Equity Participant, in, to and under the Assigned Property*]. The disclaimer of representations and warranties set forth in the second sentence of Section 6(b) of the Facility Lease is hereby incorporated herein as fully as if set forth at this place. [Notwithstanding the foregoing transfer and assignment of the Assigned Property to APS, the obligation of APS to make the payments provided in Section [insert applicable section: 9(c), 9(d) or 16(e)] of the Facility Lease (together with interest thereon in accordance with Section 3(b) of the Facility Lease) (or to make other payments in a like amount) shall not be deemed to be canceled or discharged but shall continue until all such amounts are so received by Equity Participant pursuant to the provisions of Section 7(b)(4) of the Participation Agreement.*] [The Equity Participant hereby acknowledges receipt of \$_____ representing payment in full of all amounts due to the Equity Participant under Section [insert applicable section: 9(c), 9(d) or 16(e)] of the Facility Lease.**]

ARTICLE III

EFFECTIVENESS OF TRANSFER

SECTION 3.01. Effectiveness of Transfer. The transfer of the Assigned Property shall become effective without further action upon the execution and delivery by the Equity Participant to APS of this Bill of Sale and Assignment and the furnishing of a counterpart of this Bill of Sale and Assignment to the Owner Trustee.

* To be inserted if on the date of the transfer the Equity Participant has not received the payments provided for in Section 9(c), 9(d) or 16(e) of the Facility Lease, as the case may be.

** To be inserted if on the date of the transfer the Equity Participant has received the payments provided for in Section 9(c), 9(d) or 16(e) of the Facility Lease, as the case may be.

ARTICLE IV

MISCELLANEOUS

SECTION 4.01. Successors and Assigns. This Bill of Sale and Assignment shall be binding upon the Equity Participant and its successors and shall inure to the benefit of APS and its successors and assigns.

SECTION 4.02. Governing Law. This Bill of Sale and Assignment shall be governed by and construed and enforced in accordance with the law of the State of New York.

IN WITNESS WHEREOF, the undersigned has caused this Bill of Sale and Assignment to be duly executed as of the day and year written above.

[SECURITY PACIFIC CAPITAL
LEASING CORPORATION]

By _____
Title:

APPENDIX C
to
PARTICIPATION AGREEMENT

SECTION 48(d) ELECTION

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended (the Code), and sections 1.48-4(f) and 1.1502-77(a) of the Income Tax Regulations promulgated under the Code (the Regulations), SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation (the Equity Participant), as beneficiary of a trust created by a Trust Agreement, dated as of August 1, 1986, between the Equity Participant and THE FIRST NATIONAL BANK OF BOSTON, as Owner Trustee (the Owner Trustee or the Lessor), _____, a _____ corporation as the common parent of affiliated group of corporations of which Equity Participant is a member (the Common Parent) and the Owner Trustee, hereby elect to treat ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), as lessee under a Facility Lease, dated as of August 1, 1986 (the Facility Lease), between the Owner Trustee, as Lessor, and APS, as Lessee, as having acquired the property described below for purposes of the credit allowed by sections 38 and 46(a)(1) of the Code.

(i) The name, address and taxpayer account number of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are as follows:

(a) Security Pacific Capital Leasing Corporation, Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. Taxpayer account number: 94-2960964.

(b) Common Parent.

(c) The First National Bank of Boston, as Owner Trustee, 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate

Trust Division. Taxpayer account number:

(d) Arizona Public Service Company, 411 North Central Avenue, Phoenix, Arizona 85004. Taxpayer account number [TAX I.D. No.].

(ii) The district director's offices with which the income tax returns of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are filed are as follows:

(a) Security Pacific Capital Leasing Corporation: Fresno, California.

(b) Common Parent.

(c) First National Bank of Boston, as Owner Trustee:

(d) Arizona Public Service Company: [DISTRICT DIRECTOR/LESSEE].

(iii) The property with respect to which the election is being made is an undivided interest in Palo Verde Nuclear Generating Station, Unit 2, having a fair market value of [MKT. VALUE/UNDIVIDED INTEREST].

(iv) The date on which possession of the property is transferred to the Lessee is August 18, 1986.

(v) The property is "10-year property" within the meaning of section 168(c)(2)(C) of the Code, and the estimated useful life category of the property in the hands of the Lessor is seven years or more.

(vi) Pursuant to section 48(d)(1)(A) of the Code and section 1.48-4(c)(2)(i) of the Regulations, the Lessee is treated as having acquired the leased property for an amount equal to the fair market value of property on the date possession is transferred to the Lessee.

(vii) Neither the Equity Participant, the Common Parent nor the Owner Trustee is itself a lessee with respect to the property.

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By _____
K.T. Rose,
Senior Vice President

THE FIRST NATIONAL BANK OF
BOSTON, as Owner Trustee

By _____
Martin P. Henry
Assistant Vice President

Date: August 18, 1986.

[COMMON PARENT]

By _____

CONSENT TO ELECTION

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended, and sections 1.48-4(f)(1) and 1.48-4(h) of the Income Tax Regulations promulgated thereunder, ARIZONA PUBLIC SERVICE COMPANY, as Lessee under the Facility Lease described within, hereby consents to the foregoing Section 48(d) Election.

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Paul A. Williams II,
Vice President and Treasurer

Date: August 18, 1986

APPENDIX D
to
PARTICIPATION AGREEMENT

SUMMARY STATEMENT
under
SECTION 48(d)

Pursuant to section 48(d)(1) of the Internal Revenue Code of 1954, as amended (the Code), and section 1.48-4(j) of the Income Tax Regulations promulgated thereunder, SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation (the Equity Participant), as beneficiary of a trust created by a Trust Agreement, dated as of August 1, 1986, between the Equity Participant and THE FIRST NATIONAL BANK OF BOSTON, as Owner Trustee (the Owner Trustee or the Lessor), _____, a _____ corporation, as the common parent of an affiliated group of corporations of which the Equity Participant is a member (the Common Parent), and the Owner Trustee, hereby make this Summary Statement with respect to their election to treat ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), as lessee under a Facility Lease, dated as of August 1, 1986, between the Owner Trustee, as Lessor, and APS, as Lessee, as having acquired the property described below for purposes of the credit allowed by sections 38 and 46(a)(1) of the Code.

(i) The name, address and taxpayer account number of the Equity Participant, the Common Parent, the Owner Trustee and the Lessee are as follows:

(a) Security Pacific Capital Leasing Corporation, Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. Taxpayer account number: 94-2960964.

(b) Common Parent.

(c) The First National Bank of Boston, as Owner Trustee, 100 Federal Street, Boston, Massachusetts 02110, Attention: Corporate

Trust Division. Taxpayer account number:

(d) Arizona Public Service Company, 411
North Central Avenue, Phoenix, Arizona 85004.
Taxpayer account number [TAX I.D. No.].

(ii) The property to which this Summary Statement is made is an undivided interest in Palo Verde Nuclear Generating Station, Unit 2, having a fair market value of \$141,250,000.00. The property is "10-year property" within the meaning of section 168(c)(2)(C) of the Code, and the estimated useful life category of the property in the hands of the Lessor is seven years or more.

1. The effectiveness of Section 6.11 of the Indenture is suspended in its entirety and the following provisions shall apply in lieu thereof:

Except as otherwise provided in this Section, but notwithstanding any contrary or inconsistent provision of the Indenture, subject, however, to Section 10.2 of the Indenture, (a) at all times prior to the occurrence of an Indenture Event of Default, the Owner Trustee shall retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree or consent to any amendment to, or any waiver, discharge or termination of, or give any consent under any term or provision of Sections 2(c), 3(g), 4, 7, 8(f) (iv), 9(i), 11, 15(i) (x), (i) (y), (vii) and (x) and the provisions relating to the redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease; and, provided, further, that the Owner Trustee shall, in any event, observe and perform its covenants contained in clause (iv) of Section 6.1 of the Indenture; and, provided, further, that during the continuance of any Event of Default the Owner Trustee shall promptly provide the Indenture Trustee with notice or copies of any notice, consent, waiver or approval given or received and any other action taken under clause (a); (b) upon and for a period not to exceed 60 days after the occurrence of an Indenture Event of Default described in clause (y) of paragraph (a) of Section 6.3 of the Indenture, (i) the Owner Trustee and the Agent shall consult and cooperate in good faith, and, the Owner Trustee and the Indenture Trustee shall act or refrain from acting concurrently, in exercising all rights, powers and remedies of each arising under the Facility Lease and the Indenture, respectively, in all instances with a view to protecting and preserving the respective rights and remedies of the Owner Trustee and

the Holders of the Notes under the Facility Lease and the Indenture and, to the extent reasonably practicable, maximizing the prospects of recovery; without limiting the generality of the foregoing, the Owner Trustee and Indenture Trustee shall jointly exercise all rights enumerated in clause (a) above; (c) upon and at all times after the occurrence of an Indenture Event of Default described in clause (x) (ii) of paragraph (a) of Section 6.3 of the Indenture or under the circumstances described in clause (x) (i) of such paragraph, the Indenture Trustee shall have, and may freely exercise, to the exclusion of the Owner Trustee, all rights enumerated in clause (a) above and under the Indenture; provided however, that nothing in this Section shall be deemed or construed to require the Owner Trustee or Indenture Trustee to act or refrain from acting in violation of Applicable Law, nor shall the exercise of any rights, powers and remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee as defined in the ANPP Participation Agreement. Notwithstanding any provision of this Section to the contrary (other than the proviso to the preceding sentence), the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the "Stated Price") and (iii) Owner Trustee shall not have notified the Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date within 60 days after the date of such notice of election. If the Owner Trustee shall fail timely to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate to any Person (other than the Indenture Trustee, Agent or any Holder(s) or Affiliates of any thereof) at a price no lower than the Stated Price at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the Stated Price, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all of the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate. At any time after the

termination of the Facility Lease or expiration of the 180 day period described in the second preceding sentence, the Indenture Trustee may exercise any right under Applicable Law to dispose of any interest in the Lease Indenture Estate, free of any right of the Owner Trustee to purchase the same.

2. Notwithstanding anything to the contrary contained in Section 6.8(c) of the Indenture, the Owner Trustee shall not terminate the Facility Lease or arrange for the substitution of another Person as lessee under a new lease without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

3. Notwithstanding anything to the contrary contained in Section 2.3 of the Indenture, there shall be no release of all or any portion of the Lease Indenture Estate from the security or other interest created by Section 2.1 of the Indenture without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

4. If at the time any Special Transfer is effected, the Lessee shall not have assumed the obligations under the Initial Series Notes, any subsequent breach by Lessee of its covenants contained in Section 10(b)(3)(vii) of the Participation Agreement shall be an event of Default and an Indenture Event of Default.

5. Any failure by the Owner Trustee to pay the Initial Series Notes in full when and as required by Section 13(d) or Section 14(b) or 14(c) shall be an Indenture Event of Default.

6. The provisions of this Annex A shall prevail to the extent they are inconsistent with or contrary to the provisions of any of the Transaction Documents.

7. The provisions of this Annex A shall remain in full force and effect until the full payment of all principal of and premium, if any, and interest on the Initial Series Notes.

AMENDMENT NO. 1

dated as of November 1, 1986

to

PARTICIPATION AGREEMENT

dated as of August 1, 1986

among

SECURITY PACIFIC CAPITAL LEASING CORPORATION,
as Equity Participant

BANK OF AMERICA
NATIONAL TRUST AND SAVING ASSOCIATION,
for itself and as Agent for the Original
Loan Participants under the Bank Agency
Agreement, as Agent

PVNGS FUNDING CORP., INC.,
as Funding Corporation

THE FIRST NATIONAL BANK OF BOSTON,
in its individual capacity and as Owner Trustee
under a Trust Agreement,
dated as of August 1, 1986,
with the Equity Participant, as Owner Trustee

CHEMICAL BANK,
in its individual capacity and as Indenture Trustee
under a Trust Indenture, Mortgage, Security Agreement
and Assignment of Facility Lease, dated as of
August 1, 1986,
with the Owner Trustee, as Indenture Trustee

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

AMENDMENT NO. 1, dated as of November 1, 1986, to the Participation Agreement, dated as of August 1, 1986, among SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation (the Equity Participant), BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, for itself (Bank of America) and as agent for the Original Loan Participants (the Agent), PVNGS FUNDING CORP., INC., a Delaware corporation (Funding Corp.), THE FIRST NATIONAL BANK OF BOSTON, a national banking association, in its individual capacity (FNB) and as Owner Trustee (the Owner Trustee) under a Trust Agreement, dated as of August 1, 1986, with the Equity Participant, CHEMICAL BANK, a New York banking corporation, in its individual capacity (Chemical) and as Indenture Trustee (the Indenture Trustee) under a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, with the Owner Trustee, and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee).

W I T N E S S E T H :

WHEREAS, the Equity Participant, the Agent, Funding Corp., the Owner Trustee, the Indenture Trustee and the Lessee have previously entered into a Participation Agreement dated as of August 1, 1986 (the Participation Agreement);

WHEREAS, the Initial Series Notes were issued by the Owner Trustee in connection with the acquisition of the Undivided Interest and the Real Property Interest;

WHEREAS, Section 2(d) of the Participation Agreement provides for a refunding of the Initial Series Notes upon the satisfaction of the conditions set forth in Sections 2(d), 2(e) and 11(c) of the Participation Agreement;

WHEREAS, Section 3(d) of the Facility Lease provides for an adjustment to Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event of a Change in Tax Law;

WHEREAS, the parties hereto wish to refund the Initial Series Notes;

WHEREAS, such refunding of the Initial Series Notes necessitates this Amendment No. 1 to Participation Agreement (Amendment No. 1);

WHEREAS, Section 10.1(viii) of the Indenture provides, among other things, that the Owner Trustee and Indenture Trustee may, without consent of the Holders of Notes Outstanding, execute a supplement to the Indenture in order to evidence the issuance of and to provide the terms of Additional Notes;

WHEREAS, the Owner Trustee and the Indenture Trustee intend to execute Supplemental Indenture No. 1, dated as of November 1, 1986 (Supplemental Indenture No. 1), to the Indenture, providing for the issuance under the Indenture of the Refunding Notes (as defined in Supplemental Indenture No. 1) and amending certain provisions thereof and Appendix A thereto;

WHEREAS, Section 10.2(ii) of the Indenture provides, among other things, that, upon receipt of a written instruction from the Lessee and the Owner Trustee, the Indenture Trustee shall consent to certain amendments to the Facility Lease and the Assignment and Assumption;

WHEREAS, the Owner Trustee and the Lessee intend to execute Amendment No. 1, dated as of November 1, 1986 (Lease Amendment No. 1), to the Facility Lease, to amend certain provisions thereof, Appendix A thereto and certain schedules thereto; and

WHEREAS, the Owner Trustee and the Lessee intend to execute Amendment No. 1, dated as of November 1, 1986 (Assignment and Assumption Amendment No. 1), to the Assignment and Assumption, to amend Appendix A thereto;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

Except as otherwise defined herein and in the recitals, capitalized terms used herein shall have the respective meanings set forth in Appendix A to the Participation Agreement.

SECTION 2. Agreement of Funding Corp.

Subject to the terms and conditions hereof and of Sections 2(d), 2(e) and 11(c) of the Participation Agreement, on the Refunding Date, Funding Corp. shall make a Refunding Loan to the Owner Trustee by paying to the Indenture Trustee immediately available funds in an amount equal to \$113,000,000.

SECTION 3. Issuance of Refunding Notes by Owner Trustee; Application of Proceeds.

Subject to the terms and conditions hereof and of Sections 2(d), 2(e) and 11(c) of the Participation Agreement and Section 3.5 of the Indenture, on the Refunding Date, upon receipt of the Refunding Loan to be made by Funding Corp. in accordance with Section 2 hereof, the Indenture Trustee, at the direction of the Owner Trustee, shall (a) authenticate and deliver the Refunding Notes, in the aggregate principal amount of the Refunding Loan and bearing interest at the rates per annum and in the amounts, respectively, set forth in, or determinable under, the Indenture and (b) apply the proceeds of the Refunding Loan to the prepayment in full of the principal of the Initial Series Notes. Notwithstanding any provision of the Participation Agreement or the Facility Lease to the contrary, it is understood and agreed that additional adjustments pursuant to Section 3(d) of the Facility Lease may be made at one time during the year commencing November 20, 1986 and no more frequently than annually thereafter.

SECTION 4. Implementation.

(a) Forms. The forms of Supplemental Indenture No. 1, Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 are attached hereto as Exhibits A, B and C, respectively.

(b) Request by the Equity Participant. In accordance with Section 2.01 of the Trust Agreement, the Equity Participant hereby requests that the Owner Trustee (i) execute and deliver this Amendment No. 1, Supplemental Indenture No. 1, Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 (collectively, the Refunding Amendments), (ii) execute the Refunding Notes and request the Indenture Trustee to authenticate and deliver the Refunding Notes pursuant to Section 3.5(2) of the Indenture and (iii) execute and

deliver all other agreements, instruments and certificates contemplated by the Transaction Documents, the Financing Documents and the Refunding Amendments.

(c) Instruction and Consent. In accordance with Section 10.2 of the Indenture, the Lessee and the Owner Trustee hereby instruct the Indenture Trustee to consent to Lease Amendment No. 1 and Assignment and Assumption Amendment No. 1 and the Indenture Trustee so consents. In accordance with Section 10.1 of the Indenture, the Owner Trustee and the Indenture Trustee hereby consent and agree to execute Supplemental Indenture No. 1.

(d) Recordations and Filings. The Lessee agrees that it will cause to be made the recordations and filings set forth in Schedule 1 hereto and that such filings and recordations are all the recordations and filings that are necessary in order to preserve, protect and perfect the Owner Trustee's rights and interests under the Facility Lease, as amended by Lease Amendment No. 1, and the first and prior security interest of the Indenture Trustee in the Lease Indenture Estate under the Indenture, as amended by Supplemental Indenture No. 1.

SECTION 5. Conditions Precedent.

(a) Conditions Precedent to Obligations of Funding Corp. The obligations of Funding Corp. to take the actions specified in Section 2 with respect to the Owner Trustee on the Refunding Date shall be subject to the following conditions precedent:

(i) each of the Underwriting Agreement dated November 6, 1986 (the "Underwriting Agreement") and the Terms Agreement dated November 6, 1986 (the "Terms Agreement") among Funding Corp., the Lessee, and The First Boston Corporation, Kidder, Peabody & Co. Incorporated and Salomon Brothers Inc, individually and as representatives of the several underwriters identified therein (collectively, the "Underwriters") relating to the offer and sale to the public of \$273,000,000 aggregate principal amount of Secured Lease Obligation Bonds Series 1986 of Funding Corp. (the "Bonds") shall have been executed and delivered;

(ii) the Underwriters shall have purchased the Bonds pursuant to, and in accordance with the terms of, the Underwriting Agreement and the Terms Agreement;

(iii) there shall have been delivered to Funding Corp., the Indenture Trustee and the Lessee copies of the opinions delivered to the Underwriters pursuant to Sections 5(d), 5(e), 5(f) and 5(g) of the Underwriting Agreement; and

(iv) the conditions of the obligations of the Underwriters set forth in Sections 5(a), 5(b), 5(c), 5(d), 5(e), 5(f), 5(g), 5(i) and 5(j) of the Underwriting Agreement shall have been met.

(b) Conditions Precedent to Obligations of the Owner Trustee. The obligations of the Owner Trustee to issue and deliver the Refunding Notes to Funding Corp. on the Refunding Date in consideration of the Refunding Loan shall be subject to performance by Funding Corp. of its obligations under Section 2 hereof.

(c) Conditions Precedent to Obligations of the Indenture Trustee. The obligations of the Indenture Trustee to take the action required by Section 3 hereof on the Refunding Date shall be subject to fulfillment of the conditions set forth in Section 3.5 of the Indenture.

SECTION 6. Amendments.

(a) Section 8(c)(5) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in clause (ii) of Section 8(c)(5).

(b) Section 10(a)(5) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in clause (vi) of Section 10(a)(5).

(c) Section 10(a)(6) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the second use of the phrase "Undivided Interest" in Section 10(a)(6).

(d) Section 10(b)(3)(ii)(A) of the Participation Agreement is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 10(b)(3)(ii)(A).

(e) Section 10(b)(3)(viii) of the Participation Agreement is amended in its entirety as follows:

"(viii) Decommissioning. (A) Unit 2, the Common Facilities used in respect of Unit 2, the other property included in the Unit 2 Retained Assets and allocable to Unit 2 and the portion of the PVNGS Site allocable to Unit 2 shall be decommissioned and retired from commercial service in accordance with Applicable Law and, to the extent a method of decommissioning is not prescribed by Applicable Law, by the method for decommissioning determined as provided in the ANPP Participation Agreement (the foregoing being herein referred to as Decommissioning).

(B) As between the Lessee, the Owner Trustee, the Equity Participant, each Loan Participant and any transferee (including by way of lease) or assignee of any of the Lessor's or the Equity Participant's right, title or interest in Unit 2 (all such Persons being herein referred to as Decommissioning Beneficiaries), the Lessee agrees to pay, be solely responsible for, and to indemnify such parties against, all costs and expenses relating or allocable to, or incurred in connection with, Decommissioning (but, in the case of any such transferee or assignee who becomes a "Participant", as defined in the ANPP Participation Agreement, only to the extent of the Unit 2 Interest) (all such costs and expenses, to the extent of a 29.1% interest in Unit 2, being herein referred to as Decommissioning Cost), notwithstanding (i) the occurrence of the Lease Termination Date, any Default, Event of Default, Event of Loss, Deemed Loss Event or any other event or occurrence, (ii) any provision of any Transaction Document, or other document, instrument or agreement, including the ANPP Participation Agreement, (iii) any provision of the License or any other license or permit, or (iv) any

Applicable Law, either now or hereafter in effect, charter or by-law provision, Governmental Action or other impediment, including, without limitation, the bankruptcy or insolvency of the Lessee; it being understood that (x) the obligations of the Lessee under this clause (B) are and shall be absolute, unconditional and irrevocable and (y) the obligations of the Lessee under this clause (B) shall not extend to any interest of any Decommissioning Beneficiary acquired other than as a Decommissioning Beneficiary hereunder. Insofar as the obligations of the Lessee under this clause (B) relate to the portion of Unit 2 in excess of the Unit 2 Interest the Lessee shall be subrogated to the rights, if any, of the Decommissioning Beneficiaries against other Persons in respect of such portion of Decommissioning, provided that the Lessee shall not exercise any right to which it has been subrogated in any manner materially adverse to the Decommissioning Beneficiaries. (C) The Lessee shall use its best efforts to cause the ANPP Administrative Committee to use the safest and most reliable method of Decommissioning consistent with public health and safety. (D) The Lessee shall establish a special decommissioning trust fund or funds (the Decommissioning Trust Fund) for the accumulation and full funding of amounts sufficient by December 31, 2015 to pay Decommissioning Cost. For this purpose, Decommissioning Cost shall be as determined by an expert selected by the Equity Participant and reasonably acceptable to the Lessee (the Decommissioning Expert). For purposes of making such determination, such expert shall assume that the method of Decommissioning Unit 2 shall be the costlier of (i) the DECON method of decommissioning (if not prohibited by Applicable Law), plus cost of removal, or (ii) the method of decommissioning required under Applicable Law. The Decommissioning Trust Fund shall be created as promptly as practicable after the Closing Date by the execution and delivery of the Decommissioning Trust Agreement. The Decommissioning Trust Fund shall be funded by the making of semi-annual deposits in the Decommissioning Trust

Fund (with the first such semi-annual deposit to be made on or before the fifth anniversary of the Closing Date) by the Lessee in such amounts as would, based on investments in such securities as are permitted under the Decommissioning Trust Agreement and utilizing the actuarial assumptions used by the Lessee as of the Closing Date for its pension fund, as such assumptions may be changed from time to time by the Lessee with the consent of the Equity Participant, result in the Decommissioning Trust Fund being funded by December 31, 2015 in the full amount of the Decommissioning Cost; provided, however, that such actuarial assumptions shall reflect that earnings on amounts deposited in the Decommissioning Trust Fund shall be subject to Federal income taxation until such time that under Applicable Law such earnings on such amounts will not be subject to Federal income taxation. During the first 25 years after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert every five years. Commencing in the 26th year after the Closing Date, Decommissioning Cost will be reviewed by the Decommissioning Expert each year. Immediately following each such determination by the Decommissioning Expert prior to December 31, 2015, the Lessee will make appropriate adjustments, if required, in its semi-annual deposits to be made thereafter so that, based on the investment and actuarial assumptions then in effect with respect to the Decommissioning Trust Fund, such Fund will be funded in the full amount of the Decommissioning Cost as so determined by December 31, 2015. During the first 20 years following the Closing Date, the Decommissioning Trust Fund will be invested and reinvested in accordance with standards no more liberal than the investment guidelines and actuarial assumptions set forth in the Decommissioning Trust Agreement. Commencing in the 21st year following the Closing Date and thereafter, the Decommissioning Trust Fund will be invested and reinvested in Decommissioning Fund Permitted Investments; provided, however, that in no event shall the Decommissioning Trust Fund be invested in any

securities of the Lessee or any Affiliate thereof. The Decommissioning Trust Fund shall be the fund of the Lessee, provided that the Lessor shall be granted and shall have a security interest in such fund as security for the obligations of the Lessee under this Section 10(b)(3)(viii). If, after the Decommissioning of Unit 2, there shall be any funds remaining in the Decommissioning Trust Fund, such funds shall be the property of, and be paid to, the Lessee. (E) In the event that (i) the Facility Lease shall have expired or terminated on or after December 31, 2015, (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default) and (ii) thereafter the Lessor shall (1) release the Undivided Interest to any Person or (2) retain the Undivided Interest and sell power and energy from its Generation Entitlement Share, then after the Lessor has received (x) in the case of clause (1) above, net rents (after reduction for expenses incurred by the Lessor in connection therewith) in an aggregate amount (when discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) equal to 23.5% of Facility Cost, as adjusted to reflect inflation or deflation from the Closing Date to the time of determination (the Adjusted Base Amount)-, or (y) in the case of clause (2) above, net electric revenues (after reduction for expenses incurred by the Lessor in earning such revenues) in an aggregate amount (discounted as aforesaid) equal to the Adjusted Base Amount, the Lessor shall thereafter reimburse the Lessee out of any further net rent received or net proceeds received from the sale of power and energy to the extent that such rent or proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2 (payable on an annual basis with respect to each year or portion thereof during the term of such lease referred to in clause (1) above or such period referred to in clause (2) above during which

the Lessor retains the Undivided Interest); provided, however, that when such amount has been paid the Lessor shall have no further obligation to make reimbursement to the Lessee pursuant to this Section 10(b)(3)(viii). (F) In the event that (i) the Facility Lease shall have expired or terminated on or after December 31, 2015 (other than in connection with an Event of Loss, Deemed Loss Event or Event of Default), (ii) the Lessor shall sell the Undivided Interest to any Person (including the Lessee in connection with the exercise by the Lessee of the purchase option provided by Section 13(c) of the Facility Lease), and (iii) the net sales proceeds (discounted back to the Lease Termination Date at a rate per annum equal to the Prime Rate as of the Lease Termination Date) received by the Lessor in connection therewith shall exceed the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above), then the Lessor shall reimburse the Lessee out of the net proceeds of such sale, to the extent that such proceeds are attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date through the remaining economic useful life of Unit 2, whereupon the reimbursement obligation of the Lessor under this Section 10(b)(3)(viii) shall terminate; provided, however, that any such reimbursement shall not reduce the amount of such net sales proceeds retained by the Lessor to an amount (discounted as aforesaid) equal to less than the Adjusted Base Amount (reduced by the net amounts, if any, actually realized by the Lessor pursuant to clause (E) above). The reimbursement obligations of the Lessor under clauses (E) and (F) of this Section 10(b)(3)(viii) are for the sole benefit of the Lessee, and no other Person shall be a third party beneficiary with respect thereto. For purposes of this Section 10(b)(3)(viii), (x) the amount of net rents, net revenues and net sales proceeds attributable to the decommissioning obligation of the Lessee shall be the amount by which

such rents, revenues and proceeds are greater than they would have been if the Lessee had had no such obligation, and (y) the amount thereof attributable to the period after the Lease Termination Date shall be the amount determined in the immediately preceding clause (x) multiplied by a fraction the denominator of which is the number of months in the period commencing May 20, 1986, and ending on the expiration of the economic useful life of Unit 2 as estimated at the time a determination is being made pursuant to this Section 10(b)(3)(viii) and the numerator of which is the number of months in the period commencing on the Lease Termination Date and ending on the expiration of such economic useful life. In the event that the Lessee and the Lessor shall not agree as to the amount of net rents, net electric revenues or net sales proceeds attributable to the decommissioning obligation of the Lessee under this Section 10(b)(3)(viii) with respect to the period from and after the Lease Termination Date, such amount shall be determined by the Appraisal Procedure. (G) Upon presentation of evidence by the Lessee, reasonably satisfactory to the Equity Participant and the Owner Trustee, that there are amounts then due to pay Decommissioning Cost, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to be delivered pursuant to the Decommissioning Trust Agreement for payment of Decommissioning Cost. (H) Upon presentation of a certificate of a nuclear expert selected by the Lessee and reasonably satisfactory to the Equity Participant and the Owner Trustee, stating that Decommissioning has been completed and all costs and expenses relating or allocable to, or incurred in connection with, Decommissioning have been paid in full, the Equity Participant and the Owner Trustee agree to execute such certificates as may be required to release any funds then remaining in the Decommissioning Trust Fund. (I) Notwithstanding anything in this Participation Agreement or any other Transaction Document to the contrary, the Equity Participant, the Owner Trustee and the

Lessee agree to cooperate in amending this Participation Agreement and the Decommissioning Trust Agreement to the extent necessary to enable the Decommissioning Trust Agreement to comply with Section 468A of the Code, or to establish a separate fund meeting the requirements of said Section 468A; provided, however, that in no event shall any such amendment have a material adverse effect on the Equity Participant's rights in Unit 2 or its security interest in the Decommissioning Trust Fund."

(f) Section 14(a) of the Participation Agreement is amended hereby (i) by adding the phrase "and the last sentence of Section 3(b)" after the phrase "this Section 14" in both places where it appears, (ii) by adding the phrase "the law firms referred to in clause (i) above," before the phrase "White & Case" in clause (v) of Section 14(a) and (iii) by replacing the last paragraph of Section 14(a) in its entirety as follows:

"To the extent not included in Closing Date Transaction Expenses which are disbursed as provided in Section 4(a)(i), the Owner Trustee shall pay or shall cause others to be reimbursed for, in each case with funds provided by the Equity Participant, an appropriate portion of Transaction Expenses for which invoices or other requests for payment are received on or prior to March 31, 1987."

(g) Section 14(b) (ii) of the Participation Agreement is amended hereby by deleting the phrase "including, without limitation, legal and other professional fees and expenses incurred by Agent" and by adding the word "Agent," before the phrase "the Loan Participants".

(h) Section 17(a) of the Participation Agreement is amended hereby by adding the phrase "and related definitions" before the period at the end of the second sentence of Section 17(a).

(i) Since the parties to the Participation Agreement are, by executing this Amendment No. 1 and Lease Amendment No. 1, complying with Sections 19(k) and

19(1) of the Participation Agreement; those sections are hereby deleted.

(j) Appendix A to the Participation Agreement is hereby deleted in its entirety and replaced with Appendix A hereto.

SECTION 7. Miscellaneous.

(a) Execution. This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Governing Law. This Amendment No. 1 has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the law of the State of New York.

(c) Responsibility For Recitals. The recitals contained herein shall be taken as the statements of the Lessee, and the other parties hereto assume no responsibility for the correctness of the same.

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to the Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By W. J. R.
Senior Vice President

Date: November 19, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Original
Loan Participants

By _____
Title:

By _____
Assistant Vice President

Date: November , 1986

PVNGS FUNDING CORP., INC.

By _____
Vice President

Date: November , 1986

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to the Participation Agreement to be duly executed by their respective officers thereunto duly authorized as of the dates set forth below.


SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By _____
Senior Vice President

Date: November , 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION, for itself and
as Agent for the Original
Loan Participants

By  _____
Title: Group Vice President

By  _____
Assistant Vice President

Date: November 19 , 1986

PVNGS FUNDING CORP., INC.

By  _____
Vice President


Date: November 19 , 1986

ARIZONA PUBLIC SERVICE
COMPANY

By 
Vice President and Treasurer

Date: November 17, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner
Trustee

By: 
Authorized Officer
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK, in its indi-
vidual capacity and as
Indenture Trustee

By 
Vice President

Date: November 17, 1986

Schedule 1
to
Amendment No. 1
to
Participation Agreement

RECORDATIONS AND FILINGS

Part I. Recordations in Respect to the Sale of, and Owner Trustee's Title to, the Undivided Interest and the Real Property Interest.

County Recorder, Maricopa County, Arizona:

- (i) Lease Amendment No. 1;
- (ii) Supplemental Indenture No. 1 to the Indenture; and
- (iii) Assignment and Assumption Amendment No. 1.

Part II. Filings UCC-2 Financing Statements.

(a) Separate financing statement amendments naming Arizona Public Service Company, as lessee, the Owner Trustee, as lessor, and the Indenture Trustee, as assignee of the Owner Trustee, with respect to the Facility Lease, as amended by Lease Amendment No. 1, were filed in the records of:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986 (regular and public utility filings); and
- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

(b) Separate financing statement amendments naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, and listing, as collateral covered thereby, the Lease Indenture Estate, were filed in the records of:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986;
and
- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

(c) A financing statement amendment naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, and listing, as collateral covered thereby, the Lease Indenture Estate, was filed on November 19, 1986, with the Secretary of State of the Commonwealth of Massachusetts and the Boston Town Clerk.

Part III. Filings UCC-1 Financing Statements.

Financing statements naming Funding Corp., as debtor, and the Collateral Trust Trustee, as secured party, and listing, as collateral covered thereby, the "Pledged Property" under the Collateral Trust Indenture, as amended and supplemented, were filed with:

- (1) the Secretary of State of the State of Arizona, on November 19, 1986;
and
- (2) the County Recorder of Maricopa County, Arizona, on November 19, 1986.

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof", "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the initial series of Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Aggregate Liability shall mean the amount of Aggregate Liability for a single Nuclear Incident of all Persons Indemnified, as determined in accordance with the Price-Anderson Act.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Adjustment Factor shall mean the quotient obtained by dividing the number of Nuclear Facilities having operating licenses by 100.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive) or accrual of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

Aggregate Liability shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "aggregate liability", the term "Aggregate Liability" shall be similarly expanded.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 13(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes, as amended.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated as of August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under the Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York or Boston, Massachusetts are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement is or is not included or reflected in the plans and specifications for Unit 2, as built, and (b) any alteration, modification, addition or

improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 2 to the Facility Lease, and (ii) during any Renewal Term, the amount equal to (A) the present value (declining in semi-annual steps over such Renewal Term and discounted at a rate of 10%) of the remaining Basic Rent payable from time to time in respect of the Undivided Interest for such Renewal Term plus (B) the present value of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term (increasing in semi-annual steps over such Renewal Term and discounted at a rate of 10%) all as set forth in a schedule to be prepared prior to the commencement of such Renewal Term. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation), of

any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean the Collateral Trust Indenture dated as of November 1, 1986, among APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS facilities which are common to all generating units, including Unit 2, at PVNGS.

Common Parent shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Current Pricing Assumptions shall mean the assumptions attached to the letter from the Lessee to the Equity Participant dated November 19, 1986, as such letter may be replaced from time to time with the consent of the Equity Participant.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Expert shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deed shall mean the Deed, dated as of August 18, 1986, from APS to the Owner Trustee.

Deemed Loss Event shall mean any of the following events (unless and until waived in writing by the Equity Participant):

(1) Utility Regulation. If at any time from and including the Closing Date and before the Lease Termination Date, the Lessor or the Equity Participant, by reason of the acquisition or ownership of the Undivided Interest or the Real Property Interest or any part thereof by the Lessor (or any beneficial interest therein by the Equity Participant) or the lease of the Undivided Interest to the Lessee or any of the other transactions contemplated by the Transaction Documents, shall be deemed by any Governmental Authority having jurisdiction to be, or shall become subject to regulation (other than Non-Burdensome Regulation) as, an electric utility, a public utility or a holding company under any Applicable Law or as a consequence of any Governmental Action, and the effect thereof on the Lessor or the Equity Participant would be, in the sole judgment of the Equity Participant, acting on the advice of counsel, adverse, except that if the Lessee, at its sole cost and expense, is contesting diligently and in good faith any Governmental Action which would otherwise constitute a Deemed Loss Event under this clause (1), such Deemed Loss Event shall be deemed not to have occurred so long as in the sole judgment of the Equity Participant (i) such

contest does not involve any danger of the foreclosure, sale, forfeiture or loss of, or the creation of any Lien on, the Undivided Interest, the Real Property Interest or any part thereof or any interest therein, (ii) such contest does not adversely affect the Undivided Interest or the Real Property Interest or any part thereof or any other property, assets or rights of the Lessor or the Equity Participant or the lien of the Indenture thereon, (iii) the Lessee shall have furnished the Equity Participant with an opinion of independent counsel satisfactory to the Equity Participant to the effect that (a) there exists a reasonable basis for contesting such determination or (b) in the case of any action arising from or related to the Lessor or the Equity Participant under the Holding Company Act, it is more likely than not that the Lessee will successfully contest such determination without the need for any appeal, (iv) such determination shall be effectively stayed or withdrawn during such contest (and shall not in the sole judgment of the Equity Participant be subject to retroactive application at the conclusion of such contest) in a manner satisfactory to the Equity Participant, and the Equity Participant shall have determined in its sole judgment that such contest and the Lessor's continued ownership of the Undivided Interest and the Real Property Interest during the pendency of such contest will not adversely affect its business or the business of any of its Affiliates, and (v) the Lessee shall have indemnified the Lessor and the Equity Participant in a manner satisfactory to the Equity Participant for any liability or loss which either may incur; it being understood, however, that the term Equity Participant as used in this clause (1) does not include any Transferee who at the time of transfer is an entity which is subject to regulation as an electric utility, public utility or a holding company under Applicable Law or Governmental Action.

(2) Change in Applicable Law. Any change in, or new interpretation by a Governmental Authority having jurisdiction relating to, Applicable Law, including, without limitation, the Price-Anderson Act, the Atomic Energy Act, the Nuclear Waste Act or the regulations of the NRC, in each case as in effect on the Closing Date, as a result of which, in the opinion of independent counsel to the Equity

Participant: (i) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified is increased; (ii) the Aggregate Liability for a single Nuclear Incident of all Persons Indemnified exceeds the amount of Financial Protection required under Applicable Law and available at the time of such Nuclear Incident; (iii) (a) the amount of Primary Financial Protection required with respect to a single Nuclear Facility under Applicable Law is increased, whether or not the total amount of Financial Protection required with respect to a single Nuclear Facility is increased, or (b) the amount of Financial Protection required under Applicable Law is increased (including, but not limited to, an increase in the amount of retrospective premiums payable under the Retrospective Rating Plan) or (c) the amount of retrospective premiums payable under the Retrospective Rating Plan in any one year with respect to two or more Nuclear Incidents is increased; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. Section 140.22 or 10 C.F.R. Section 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan) shall be modified or changed in any material respect; (v) the Lessor or the Equity Participant may become liable or responsible in any capacity (including, without limitation, through assessments imposed by a Governmental Authority) for payments owed in respect of the Nuclear Waste Fund (as such term is used in Section 302 of the Nuclear Waste Act) or in respect of the handling or disposal of nuclear waste, decontamination, storage, transportation or safekeeping of radioactive or hazardous materials or any other obligation in the nature of the foregoing; (vi) the Lessor, the Equity Participant or the Lessee may be prohibited from asserting any right, protection or defense available under Applicable Law as of the Closing Date with respect to civil or criminal actions brought in connection with a Nuclear Incident (including, without limitation, through an expansion of the waiver of defenses provision under subsection 170n. of the Atomic Energy Act); (vii) there shall be expressly created a new cause of action whereby any Person who pays or will pay retrospective premiums under the Retrospective Rating Plan or other assessments required under Applicable Law may recover the amount of such

payments from the facility at which a Nuclear Incident occurs or from any Person associated with such facility; (viii) there shall be a third tier or additional level of potential or real liability (including assessments imposed by a Governmental Authority) with respect to a Nuclear Facility; (ix) there shall be any type of claim, liability or expense (other than the costs of investigating and settling claims and defending suits for damage) excluded from the limitation of liability established by the Price-Anderson Act (through modification of the definitions of "aggregate liability", "persons indemnified", "nuclear incident" or otherwise) or excluded (or the funding or payment thereof deferred) under insurance or other Financial Protection required under Applicable Law as in effect on the Closing Date, except to the extent and in the amount expressly excluded or deferred pursuant to Applicable Law as in effect on the Closing Date; or (x) the Lessor or the Equity Participant may be exposed, during the Lease Term or after the Lease Termination Date, to any other increased real or potential liability (including, without limitation, through assessments imposed by a Governmental Authority) with respect to a Nuclear Incident or otherwise relating to the operation of PVNGS or the transactions contemplated by the Participation Agreement; provided, however, that no such change shall constitute a Deemed Loss Event if and for so long as such change or interpretation meets all the conditions constituting a Safe Harbor Change. For purposes of this clause (2), the requirement or existence of insurance, retrospective premiums, indemnities (whether by the Lessee or any other Person) or other forms of Financial Protection (similar or dissimilar to the foregoing) shall not be deemed to eliminate or negate any exposure of the Lessor or the Equity Participant to real or potential increased liability.

(3) Insurance. The Lessee shall not be in compliance with Section 10 of the Facility Lease.

(4) License. Any expiration, revocation, suspension, amendment or interpretation by any Governmental Authority of the License or any other change in Applicable Law or Governmental Action, as a result of which, prior to the Lease Termination Date, either the Lessor or the Equity Participant is

or might (i) be required to be or become a licensee under the Atomic Energy Act with respect to Unit 2 or (ii) be subject to the obligations or liabilities imposed, as of the Closing Date or thereafter, on licensees under the Atomic Energy Act with respect to Unit 2 or (iii) be otherwise subject to significant regulation.

(5) Multiple Incidents. The occurrence (i) of two or more incidents (including incidents occurring outside the United States of America), in each case at any Nuclear Facility or Facilities using a Combustion Engineering pressurized water reactor nuclear steam supply system or another nuclear steam supply system of comparable design or comparable components, the failure of which Combustion Engineering pressurized water reactor nuclear steam supply system or other nuclear steam supply system of comparable design or components results in (x) a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; (y) (A) the radiation level in the containment vessel as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor), averaged over one hour equaling or exceeding 1,000 rad per hour; or (B) any measure

of radioactivity in the primary coolant system exceeding by 1,000 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (z) damage to offsite property, including, without limitation, costs for decontamination, in amounts in excess of \$15,000,000; or (ii) within a five-year period of three or more incidents, of the type and severity described in subclause (i)(x), (y) or (z) above, at any Nuclear Facility or Facilities (including incidents occurring outside the United States of America).

(6) **Illegality; Exercise of Rights and Remedies.** Any change in Applicable Law or any Governmental Action the effect of which is or might be (i) to make any of the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law, (ii) to impede the exercise by the Lessor or the Equity Participant of any right or remedy under any Transaction Document relating to the assertion of claims for Rent or monetary damages, (iii) to cause the Lessor or the Equity Participant to be or become liable in any capacity in respect of Decommissioning, including, without limitation, all or any portion of the Termination Obligation (as defined in the ANPP Participation Agreement), or (iv) to constitute an assertion to the effect that (a) the exercise by the Lessor or the Equity Participant of any right (irrespective of the event giving rise to such right) under any Transaction Document would constitute impermissible control over Unit 2 or the licensees of Unit 2, other than an assertion consistent with the second sentence of Section 184 of the Atomic Energy Act and the NRC's regulations thereunder, including, without limitation, 10 C.F.R. Section 50.81, as now in effect, or (b) the acquisition or transfer of the Undivided Interest was in violation of, or otherwise contrary to, Applicable Law.

(7) **Violations.** With respect to PVNGS, the NRC shall have issued within a two-year period (x) two or more final orders involving "Severity Level I" violations or (y) three or more final orders involving "Severity Level I" or "Severity Level II" violations, as such terms are used in Supplement I to Appendix C to 10 C.F.R., Part 2, as in effect on the Closing Date (or, if such Supplement is amended or

superseded or different categories are in effect, comparable violations).

(8) Unit 1 and Unit 3 Incidents. (1) The occurrence of an event at Unit 1 or Unit 3 (such affected unit being herein in this definition referred to as the Affected Unit) as a result of which: (w) the radiation level in the top half of the containment vessel of the Affected Unit as measured by the average of two high range radiation monitors in the upper half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the primary coolant system of the Affected Unit shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for the Affected Unit (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of the Affected Unit's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of the Affected Unit, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date; or (2) the occurrence of a Nuclear Incident at an Affected Unit as a result of which the Affected Unit ceases to operate (or if the Affected Unit is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a

result of such Nuclear Incident) for a Period of 36 consecutive months.

(9) Radiation Level. Except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 1 or 3, the radiation level in the fuel building above either such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours.

(10) Reduced Operations. Other than in consequence of a reduction in demand, Unit 2 shall have operated in any calendar year at a net capacity factor below 35% other than as a result of a shut-down to repair damage to Unit 2; provided, however, that if the NRC shall determine at any time during the Lease Term that the operation of this paragraph might impair the ability of the Lessee or the Operating Agent to comply with the terms of the License or Applicable Law or interfere with the exercise of the NRC's jurisdiction to protect the public health and safety, then this paragraph 10 shall be deemed waived.

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its

obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank (as used herein, a Letter of Credit Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Letter of Credit Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Letter of Credit Bank, or (iii) any Letter of Credit Bank whose long-term unsecured debt securities are rated not less than Aa3 by Moody's, other than a Letter of Credit Bank to which the Equity Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of a Letter of Credit Bank which is part of a holding company structure, the failure of such Letter of Credit Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities); provided, however, that any Letter of Credit issued by a Letter of Credit Bank that is not incorporated in the United States shall provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Security Pacific Capital Leasing Corporation, and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended:

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean (i) all indemnity payments to which the Owner Trustee or the Equity Participant (or the respective successors, assigns, agents, officers, directors or employees of the Owner Trustee or the Equity Participant) is entitled, (ii) any amounts payable under any Transaction Document to reimburse the Lessor or the Equity Participant (including the reasonable expenses of the Lessor or the Equity Participant incurred in connection with any such

payment) for performing or complying with any of the obligations of the Lessee under and as permitted by any Transaction Document, (iii) any insurance proceeds with respect to an Event of Loss in excess of amounts then due and owing in respect of the principal of and premium, if any, and interest on all Notes Outstanding, (iv) any insurance proceeds (or payments with respect to risks self-insured) under liability policies, (v) any payments in respect of interest to the extent attributable to payments referred to in clauses (i) through (iv) above and (vi) if the Letter of Credit has been terminated or has expired, a portion of Casualty Value, Special Casualty Value or Extraordinary Casualty Value equal to the amount by which Modified Special Casualty Value exceeds the sum of all amounts drawn under the Letter of Credit.

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and all rights and interests with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank.

Extraordinary Casualty Value, as of any date, during the Basic Lease Term, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under the applicable provision, if any, of the Facility Lease or the Participation Agreement, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Extraordinary Nuclear Occurrence shall have the meaning assigned in Section 11 of the Atomic Energy Act and the related NRC regulations (10 C.F.R. § 140.84 and 140.85), as in effect as of the Closing Date.

Facility Cost shall mean the sum of the Purchase Price and the Real Estate Investment plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement, and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended..

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; (y) any order of or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period exceeding 24 months; or (z) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which: (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of

radioactivity in the primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) there is an assessment of core damage (according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2's containment, as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment vessel; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples) which indicates that the damage to the nuclear fuel residing in the reactor vessel is in category 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9 or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which: (x) the NRC declares to be an Extraordinary Nuclear Occurrence; (y) result in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter, (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber); provided, however, that (I) if the level of radiation constituting an Extraordinary

Nuclear Occurrence is reduced by the NRC from those set forth herein, then the levels set forth herein shall be reduced equivalently or (II) if alternative criteria for determining an Extraordinary Nuclear Occurrence are adopted by the NRC, then the criteria set forth herein shall be modified to be consistent with the criteria established by the NRC; or (z) result in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee; or of the Lessee and one or more other ANPP Participants, to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown in consequence of the occurrence of an event described in (A) clause (4) or (5) above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause (8) above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months.

Financial Protection shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "financial protection", the term "Financial Protection" shall be similarly expanded.

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meaning set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, shall mean the Generation Entitlement Share of APS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all siting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Group shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, each Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture, and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles; a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors, and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean the percentage set forth opposite "Lessor's Portion" on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the

Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended, (vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Aggregate Loss shall be computed and applied in respect of Unit 2, including all interests therein, and with respect to each calendar year shall mean the sum of (i) retrospective premiums, if any, payable during such year under the Retrospective Rating Plan with respect to any Nuclear Incident which shall have occurred prior to the date of such calculation, (ii) all uninsured liquidated amounts paid or payable during such year, and not covered by the Retrospective Rating Plan, in respect of Nuclear Incidents, and (iii) other known assessments and costs and an assumed additional amount in respect of such retrospective premiums which would be payable during such year if a Nuclear Incident, or one additional Nuclear Incident, should occur in such year.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of

(x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of the Fixed Rate Renewal Term) in each case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Lessor's Portion of the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and (iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Lessor's Portion of the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or December 31 in such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage:

Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions. The after-tax yield component of Net Economic Return will be adjusted upward by 0.1% for each 1% downward adjustment in marginal federal tax rates pursuant to a Change in Tax Law; provided, however, that the maximum upward adjustment due solely to such increase in the after-tax yield component will result in an increase of .20% in the present value of Rent (discounted semi-annually using a semi-annual discount rate equal to 5.075%).

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Net Worth Factor shall mean the quotient obtained by dividing (i) PVNGS Net Worth, as of December 31 of the year prior to the date of any calculation of Net Worth Factor, by (ii) PVNGS Net Worth, as of December 31, 1985; provided, however, that Net Worth Factor shall not be less than 1.0 in respect of any year prior to 1991.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest and the Real Property Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest and the Real Property Interest on or after the Lease Termination Date or

(iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes and Additional Notes issued from time to time under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Facility shall mean a facility designed for producing substantial amounts of electricity and having a rated capacity of 100,000 electrical kilowatts or more.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act, as in effect as of the Closing Date; provided that if the Atomic Energy Act shall be amended to expand the definition of "nuclear incident", the term "Nuclear Incident" shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Obsolescence Redemption Date shall mean (i) if any Bonds are outstanding on the related Termination Date, the date which is 25 days after such Termination Date, or if such date is not a Business Day, the next Business Day thereafter, or (ii) if no Bonds are outstanding on such Termination Date, the Termination Date.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used or by a Contract Administrator.

Original Loan Participants shall mean Bank of America and each of the other banks (the Banks) listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% per annum in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs) or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participants and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part

thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest) under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

Persons Indemnified shall have the meaning assigned in the Price-Anderson Act, as in effect as of the Closing Date; provided that if the Price-Anderson Act shall be amended to expand the meaning of the term "person indemnified", the term "Persons Indemnified" shall be similarly expanded.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No. 85-256, 71 Stat. 576 (1957), as amended to August 18, 1986 (except as otherwise expressly provided), including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 3 to the Participation Agreement.

Primary Financial Protection shall mean Financial Protection required to be maintained by each Nuclear Facility under Applicable Law, except for such amounts required to be maintained under a Retrospective Rating Plan.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Net Worth shall mean the sum of the consolidated common stockholders equity of APS, El Paso, PNM and Southern California, and their respective successors, as shown in their most recent respective audited financial statements; provided, however, that the consolidated common stockholders equity of any such Person shall not be included in the foregoing sum after (and only after) such time as such Person is not an ANPP Participant subject to the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 4(b) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed or by the ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund the Initial Series Notes or Outstanding Bonds.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean a Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of Refunding Bonds.

Registration Statement shall mean a registration statement, including all exhibits and all documents incorporated in such Registration Statement by reference, filed with the SEC under the Securities Act in connection with the offer, issue and sale of any Refunding Bonds or Refunding Notes.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(d) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent.

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Severable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Retrospective Rating Plan shall mean the industry retrospective rating plan established pursuant to the Price-Anderson Act, or any successor or similar plan established under Applicable Law.

Safe Harbor Change shall mean any Substantial Amendment, and any other change which, had it been part of the first Substantial Amendment (together with all other changes since the first Substantial Amendment) would have been a Substantial Amendment, enacted after the Closing Date, if, upon the effective date of such Substantial Amendment or other change and at all times thereafter (as shall be determined from time to time):

(A) (1) the Lessor and the Equity Participant (x) shall, as a result of such Substantial Amendment, be exempt from all real and potential liability in respect of a Nuclear Incident (Nuclear Liability) both during and after the Lease Term (unless the Equity Participant or the Lessor, as the case may be, is as of the time of a Nuclear Incident a licensee with respect to Unit 2 under the Atomic Energy Act) and (y) shall have received an opinion of independent counsel to the Equity Participant to the effect that there is no reasonable basis for a court to hold either the Lessor or the Equity Participant liable for any Nuclear Liability, both during and after the Lease Term (subject to the exception described in the parenthetical clause in clause (x) above) and (2) in the opinion of independent counsel to the Equity Participant, such Substantial Amendment meets all the conditions stated in clause (B) below; provided, however, that part (b) in subclause (i) of clause (B) shall read as follows, "(b) the product of (1) 1.75 times (2) the Net Worth Factor times (3) the product of \$6.5 billion multiplied by the Adjustment Factor***", and subclause (iii) of clause (B) shall read as follows, "Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter shall not exceed the product of (x) 1.75 times (y) .5% times (z) the product of

the Net Worth Factor times \$6.5 billion ***"; provided, further, that in the event the Equity Participant is furnished with an opinion of its independent counsel stating that, because of a change in Applicable Law, there is a significant risk that the opinion described in subclause (y) of subclause (1) above is no longer valid, then this clause (A) shall cease to be applicable; or

(B) in the event clause (A) is not applicable, as a result of such Substantial Amendment, in the opinion of independent counsel to the Equity Participant: (i) Adjusted Aggregate Liability, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed (a) the amount of Financial Protection required to be maintained by each Nuclear Facility with respect to a single Nuclear Incident or (b) the product of (1) the Net Worth Factor times (2) the product of \$6.5 billion times (3) the Adjustment Factor, and if Adjusted Aggregate Liability should exceed either (a) or (b) above the Substantial Amendment shall no longer constitute a Safe Harbor Change; (ii) the amount of Primary Financial Protection available from commercial insurance underwriters on terms substantially equivalent (in the reasonable opinion of the Equity Participant) to the terms in effect on the Closing Date under Applicable Law and required to be maintained by licensees with respect to any single Nuclear Facility shall be at least equal to the amount required under Applicable Law (which amount shall not exceed \$500 million); (iii) Maximum Aggregate Loss, on the date of enactment of the Substantial Amendment and at all times thereafter, shall not exceed the product of (x) .5% times (y) the Net Worth Factor times (z) \$6.5 billion, and if Maximum Aggregate Loss should exceed the foregoing product the Substantial Amendment shall no longer constitute a

Safe Harbor Change; (iv) the provisions of the penultimate sentence of Section 170b. of the Atomic Energy Act, 10 C.F.R. § 140.22; or 10 C.F.R. § 140.92 (as it relates to the guarantee by the NRC of defaults by licensees under the Retrospective Rating Plan), as in effect on the Closing Date, shall not have been amended or modified in any material respect; (v) the NRC shall be required to fulfill payment obligations when due from a licensee liable for damage arising out of or related to a Nuclear Incident in the event that the payment obligations of such licensee in any calendar year exceed the amount payable by such licensee in respect of such Nuclear Facility in such year under the Retrospective Rating Plan; provided, however, that the NRC shall be entitled to reimbursement through the Retrospective Rating Plan as such payments are made over time; (vi) neither the Lessee nor any other Persons Indemnified will be required to waive the defense of the statute of limitations (existing under any Applicable Law) with respect to a Nuclear Incident (except an Extraordinary Nuclear Occurrence); with respect to an Extraordinary Nuclear Occurrence such defense shall be required to be waived only as to suits instituted within 30 years after the date the Extraordinary Nuclear Occurrence which is the subject of the suit takes place and within a prescribed number of years from the date on which the claimant first knew, or reasonably could have known, of his injury or damage and the cause thereof; (vii) neither the Lessor nor the Equity Participant shall be exposed to any increased real or potential liability (including assessments imposed by a Governmental Authority) with respect to activities authorized by the Nuclear Waste Act; (viii) none of the results contemplated in subclauses (vii) and (ix) of clause (2) of the definition of Deemed Loss Event shall have occurred; (ix) neither the Lessor nor the Equity

Participant shall, in the opinion of independent counsel to the Equity Participant delivered within six months of such Substantial Amendment, be exposed to any other material increase in its real or potential liability with respect to a Nuclear Incident, either before, on or after the Lease Termination Date, except for liability arising with respect to a Nuclear Incident which takes place after the Lessor or the Equity Participant, as the case may, becomes a licensee of the NRC, and (x) neither the Lessor, the Equity Participant nor the Lessee shall be prohibited from asserting any other right, protection or defense available under Applicable Law as in effect on the Closing Date other than those rights, protections and defenses which are waived pursuant to this definition of Safe Harbor Change; provided, however, that an expansion of the waiver of defenses provision of subsection 170n.(1) of the Atomic Energy Act so that such waivers are applicable with respect to an Extraordinary Nuclear Occurrence arising out of or resulting from or occurring in the course of (a) transportation of source material, byproduct material, or special nuclear material to or from any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, (b) activities undertaken by the Secretary, including but not limited to activities related to the storage or disposal of high-level radioactive waste, or (c) the construction, possession or operation of any facility licensed under Section 53, 63 or 81 of the Atomic Energy Act, shall not be deemed to expose the Lessor, the Equity Participant or the Lessee to any increased real or potential liability.

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor, the Equity

Participant and the Indenture Trustee in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Secretary shall mean the Secretary of Energy.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 20(a) of the Participation Agreement.

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount equal to (A) the present value (declining in semi-annual steps over such Renewal Term and discounted

at a rate of 10%) of the remaining Basic Rent payable from time to time in respect of the Undivided Interest for such Renewal Term plus (B) the present value of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term (increasing in semi-annual steps over such Renewal Term and discounted at a rate of 10%) all as set forth in a schedule to be prepared prior to the commencement of such Renewal Term. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted securities ratings.

Summary Statement shall have the meaning set forth in Section 20(b) of the Participation Agreement.

Substantial Amendment shall mean any amendment to the Price-Anderson Act or the Atomic Energy Act which would constitute a Deemed Loss Event under clause (2) of the definition of Deemed Loss Event.

Substituted Lessee shall have the meaning set forth in Section 6.8(c) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the

Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Equity Participant.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property (personal or real, tangible or intangible) and stamp taxes), levies, imposts, duties, charges, assessments or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon.

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed (or ground lease contemplated by Section 10(b)(3)(xvii) of the Participant Agreement) by an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Security Pacific Capital Leasing Corporation and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp, APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale; (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common facilities); (xiii) simulator; and (xiv) oil and diesel fuel inventories; (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements; and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii)

railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth opposite "Unit 2 Retained Assets Portion" on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

TRUST AGREEMENT

dated as of August 1, 1986

between

SECURITY PACIFIC CAPITAL LEASING CORPORATION

as Equity Participant

and

THE FIRST NATIONAL BANK OF BOSTON,

as Owner Trustee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

MOFO Nuclear Trust No. 1

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TRUST AGREEMENT

TRUST AGREEMENT, dated as of August 1, 1986, between Security Pacific Capital Leasing Corporation, a Delaware corporation (the Equity Participant) and THE FIRST NATIONAL BANK OF BOSTON, a national banking association (the Owner Trustee).

W I T N E S S E T H:

WHEREAS, the Equity Participant desires to acquire the Undivided Interest and the Real Property Interest through the Trust created hereby; and

WHEREAS, The First National Bank of Boston is willing to act as Owner Trustee and to accept the Trust created hereby;

NOW, THEREFORE, in consideration of the mutual agreements herein contained and other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.01. Definitions. All capitalized terms used herein and not otherwise defined herein shall have the meanings set forth in Appendix A to the Participation Agreement. References in this Agreement to articles, sections, paragraphs and clauses are to articles, sections, paragraphs and clauses of this Agreement unless otherwise indicated.

ARTICLE II

AUTHORITY TO EXECUTE AND PERFORM VARIOUS DOCUMENTS; RATIFICATION AND CONFIRMATION; DECLARATION OF TRUST BY THE OWNER TRUSTEE

SECTION 2.01. Authority To Execute and Perform Various Documents. The Equity Participant hereby authorizes and directs the Owner Trustee (i) to execute and deliver each Transaction Document to which the Owner Trustee is to be a party and to execute and issue and request the Indenture Trustee to authenticate and deliver the Initial Series Note (each such Transaction Document, including the Initial Series Note, to be in the form approved by the Equity Participant), (ii) to execute and deliver all other agreements, instruments and certificates contemplated by the documents referred to in clause (i),

(iii) to take whatever action shall be required to be taken by the Owner Trustee by the terms of, and exercise its rights and perform its duties under, each of the documents, agreements, instruments and certificates referred to in clauses (i) and (ii) above as set forth in such documents, agreements, instruments and certificates and (iv) subject to the terms of this Agreement, to take such other action in connection with the foregoing as the Equity Participant may from time to time direct.

SECTION 2.02. Ratification and Confirmation. By certificate dated August 8, 1986 (the Section 15.6.1 Certificate), the Owner Trustee confirmed the matters required to be confirmed on the part of a lessor in a sale and leaseback transaction under Section 15.6.1 of the ANPP Participation Agreement, a copy of which certificate is attached hereto as Schedule 1. The Equity Participant, by its execution and delivery of this Agreement, ratifies and confirms the execution and delivery by the Owner Trustee of the Section 15.6.1 Certificate.

SECTION 2.03. Declaration of Trust by the Owner Trustee: The Owner Trustee hereby declares that it will hold all estate, right, title and interest of the Owner Trustee in and to the Undivided Interest, the Real Property Interest, the Transaction Documents and any other property contributed by the Equity Participant, including without limitation all amounts of Rent, insurance proceeds and requisition, indemnity or other payments of any kind, but specifically excluding any Excepted Payments (collectively, the Trust Estate), upon the trusts set forth herein and for the use and benefit of the Equity Participant.

ARTICLE III

PAYMENTS

SECTION 3.01. Payments from Trust Estate Only. All payments to be made by the Owner Trustee under this Agreement shall be made only from the income and proceeds from the Trust Estate and only to the extent that the Owner Trustee shall have received income or proceeds from the Trust Estate to make such payments in accordance with the terms hereof, except as specifically provided in Section 6.01. The Equity Participant agrees that it will look solely to the income and proceeds from the Trust Estate to the extent available for payment as herein provided and that, except as specifically provided herein, the Owner Trustee shall not be liable to the Equity Participant for any amounts payable under this Agreement and shall not be subject to any liability under this Agreement.

SECTION 3.02. Method of Payment. All amounts payable to the Equity Participant pursuant to this Agreement shall be paid or

caused to be paid by the Owner Trustee to the Equity Participant, or its nominee, by crediting the amount to be distributed to the Equity Participant to an account maintained by the Equity Participant with the Owner Trustee in immediately available funds or by transferring such amount in immediately available funds to a banking institution with bank wire transfer facilities for the account of the Equity Participant, as instructed from time to time by the Equity Participant.

ARTICLE IV

DISTRIBUTIONS

SECTION 4.01. Distributions. Subject to the terms and requirements of the Transaction Documents, all payments and amounts received by or on behalf of the Owner Trustee shall be distributed forthwith upon receipt in the following order of priority: first, so much of such payment or amount as shall be required to pay or reimburse the Owner Trustee for any fees or expenses (including reasonable attorney's fees and expenses) not otherwise paid or reimbursed to the Owner Trustee as to which the Owner Trustee is entitled to be paid or reimbursed hereunder shall be retained by the Owner Trustee; and, second, the balance, if any, of such payment or amount remaining thereafter shall be distributed to the Equity Participant.

ARTICLE V

DUTIES OF THE OWNER TRUSTEE

SECTION 5.01. Notice of Certain Events. In the event the Owner Trustee shall have knowledge of any Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event, the Owner Trustee shall give prompt written notice thereof to the Equity Participant, the Lessee, the Loan Participant and the Indenture Trustee unless such Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event no longer exists before the giving of such notice. Subject to the provisions of Section 5.03, the Owner Trustee shall take or refrain from taking such action, not inconsistent with the provisions of the Transaction Documents, with respect thereto as the Equity Participant shall direct by written instruction to the Owner Trustee. If the Owner Trustee shall have given the Equity Participant written notice of any event and shall not have received written instructions as above provided within 30 days after mailing notice of such event to the Equity Participant, the Owner Trustee may, subject to the provisions of the Transaction Documents, take or refrain from taking such action, but shall be under no duty to, and shall have no liability for its failure or refusal to, take or

refrain from taking any action with respect thereto as the Owner Trustee shall deem advisable and in the best interests of the Equity Participant. For all purposes of this Agreement, in the absence of actual knowledge of an officer in the corporate trust division of the Owner Trustee, the Owner Trustee shall not be deemed to have knowledge of any Default, Event of Default, Indenture Default, Indenture Event of Default, Event of Loss or Deemed Loss Event unless the Owner Trustee receives written notice thereof given by or on behalf of the Equity Participant, the Lessee, the Loan Participant, the Indenture Trustee or any Holder of a Note.

SECTION 5.02. Action upon Instructions. Subject to the terms of Sections 5.01 and 5.03, upon the written instructions of the Equity Participant, the Owner Trustee will take or refrain from taking such action or actions, not inconsistent with the provisions of the Transaction Documents, as may be specified in such instructions.

SECTION 5.03. Indemnification. The Owner Trustee shall not be required to take or refrain from taking any action under this Agreement or any other Transaction Document (other than the actions specified in the first sentence of Section 5.01) unless the Owner Trustee shall have been indemnified by the Lessee or, if the Owner Trustee reasonably believes such indemnity to be inadequate, by the Equity Participant, in manner and form reasonably satisfactory to the Owner Trustee, against any liability, fee, cost or expense (including reasonable attorneys' fees and expenses) which may be incurred or charged in connection therewith, other than such as may result from the willful misconduct or gross negligence of the Owner Trustee; and, if the Equity Participant shall have directed the Owner Trustee to take or refrain from taking any action under any Transaction Document, the Equity Participant agrees to furnish such indemnity by a written undertaking of indemnification and, in addition, to pay the reasonable compensation of the Owner Trustee for the services performed or to be performed by it pursuant to such direction. The Owner Trustee shall not be required to take any action under any Transaction Document if the Owner Trustee shall reasonably determine, or shall have been advised by counsel, that such action is likely to result in personal liability for which the Owner Trustee has not been and will not be adequately indemnified or is contrary to the terms hereof or of any document contemplated hereby to which the Owner Trustee is a party or is otherwise contrary to law.

SECTION 5.04. No Duties Except as Specified in Trust Agreement or Instructions. The Owner Trustee shall not have any duty or obligation to manage, control, use, make any payment in respect of, register, record, insure, inspect, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or any other part of the Trust Estate, or to otherwise take or refrain from taking any action under or in connection with any

document contemplated hereby to which the Owner Trustee is a party, except as expressly provided by the terms of this Agreement or in written instructions from the Equity Participant received pursuant to Section 5.01 or 5.02; and no implied duties or obligations shall be read into this Agreement against the Owner Trustee. The Owner Trustee nevertheless agrees that it will, in its individual capacity and at its own cost and expense, promptly take all action as may be necessary to discharge any Lessor's Liens arising by, through or under it on any part of the Trust Estate.

SECTION 5.05. No Action Except Under Specified Documents or Instructions. The Owner Trustee agrees that it will not manage, control, use, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or any other part of the Trust Estate except (i) as required by the terms of the Transaction Documents, (ii) in accordance with the powers granted to, or the authority conferred upon, the Owner Trustee pursuant to this Agreement or (iii) in accordance with the express terms hereof or with written instructions from the Equity Participant pursuant to Section 5.01 or 5.02.

SECTION 5.06. Absence of Duties. Except in accordance with written instructions furnished pursuant to Section 5.01 and 5.02, and without limitation of the generality of Section 5.04, the Owner Trustee shall not have any duty to (i) file, record or deposit any Transaction Document or any other document, or to maintain any such filing, recording or deposit or to refile, rerecord or redeposit any such document, (ii) obtain insurance on the Undivided Interest or the Real Property Interest or effect or maintain any such insurance, other than to receive and forward to the Equity Participant any notices, policies, certificates or binders furnished to the Owner Trustee pursuant to the Facility Lease, (iii) maintain Unit 2, the Undivided Interest or the Real Property Interest, (iv) pay or discharge any Tax or any Lien owing with respect to or assessed or levied against any part of the Trust Estate, except as provided in the last sentence of Section 5.04, other than to receive and forward notice of such Tax or Lien to the Equity Participant, (v) confirm, verify, investigate or inquire into the failure to receive any reports or financial statements of the Lessee, (vi) inspect Unit 2 at any time or ascertain or inquire as to the performance or observance of any of the covenants of the Lessee or any other Person under any Transaction Document with respect to the Undivided Interest, the Real Property Interest or Unit 2 or (vii) manage, control, use, sell, dispose of or otherwise deal with the Undivided Interest, the Real Property Interest or Unit 2 or any part thereof or any other part of the Trust Estate, except as provided in Section 5.05:

ARTICLE VI

THE OWNER TRUSTEE

SECTION 6.01. Acceptance of Trust and Duties. The Owner Trustee accepts the trusts hereby created and agrees to perform the same, but only upon the terms of this Agreement. The Owner Trustee also agrees to disburse all moneys actually received by it constituting part of the Trust Estate upon the terms of this Agreement. The Owner Trustee shall not be answerable or accountable under any circumstances, except for (i) its own wilful misconduct or gross negligence, (ii) the inaccuracy of any of its representations or warranties contained in Section 6.03 or under Section 8(a) of the Participation Agreement given expressly in its individual capacity, (iii) its failure to perform obligations expressly undertaken by it in the last sentence of Section 5.04 of this Agreement or in Section 8(b) of the Participation Agreement or (iv) Taxes based on or measured by any fees, commissions or compensation received by it for acting as trustee in connection with any of the transactions contemplated by the Transaction Documents.

SECTION 6.02. Furnishing of Documents. The Owner Trustee will furnish to the Equity Participant, promptly upon receipt thereof, duplicates or copies of all reports, notices, requests, demands, opinions, certificates, financial statements and any other writings furnished to the Owner Trustee hereunder or under the Transaction Documents, unless by the express terms of any Transaction Document a copy of the same is required to be furnished by some other Person directly to the Equity Participant, or the Owner Trustee shall have determined that the same has already been furnished to the Equity Participant.

SECTION 6.03. No Representations or Warranties as to the Undivided Interest, the Real Property Interest, Unit 2 or Documents. The Owner Trustee makes (i) NO REPRESENTATION OR WARRANTY AS TO THE TITLE, VALUE, CONDITION, DESIGN, OPERATION, MERCHANTABILITY OR FITNESS FOR USE OF THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST, UNIT 2 OR ANY OTHER REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, WITH RESPECT TO THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST OR UNIT 2 WHATSOEVER, except that the Owner Trustee hereby represents, warrants and covenants to the Equity Participant that it will comply with the last sentence of Section 5.04, and (ii) no representation or warranty as to the validity or enforceability of any Transaction Document or as to the correctness of any statement made by any Person other than the Owner Trustee, contained in any thereof, and except that the Owner Trustee represents, warrants and covenants to the Equity Participant that this Agreement has been and each of such other documents which contemplates execution thereof by the Owner Trustee has been or will be executed and delivered by its

officers who are, or will be, duly authorized to execute and deliver such documents on its behalf.

SECTION 6.04. No Segregation of Moneys; No Interest.

Except as otherwise provided herein or in any of the Transaction Documents, moneys received by the Owner Trustee hereunder need not be segregated in any manner, except to the extent required by law, and may be deposited under such general conditions as may be prescribed by law, and the Owner Trustee shall not be liable for any interest thereon, except as may be agreed to by the Owner Trustee.

SECTION 6.05. Reliance; Advice of Counsel. The Owner Trustee shall not incur any liability to any Person in acting upon any signature, instrument, notice, resolution, request, consent, order, certificate, report, opinion, bond or other document or paper believed by it to be genuine and believed by it in good faith to be signed by the proper party or parties. The Owner Trustee may accept a certified copy of a resolution of the board of directors or other governing body of any corporate party as conclusive evidence that such resolution has been duly adopted by such body and that the same is in full force and effect. As to any fact or matter the manner of ascertainment of which is not specifically prescribed herein, the Owner Trustee may for all purposes hereof rely on an Officers' Certificate of the relevant party as to such fact or matter, and such certificate shall constitute full protection to the Owner Trustee for any action taken or omitted to be taken by it in good faith in reliance thereon. In the administration of the trusts hereunder, the Owner Trustee may execute any of the trusts or powers hereof and perform its powers and duties hereunder directly or through agents or attorneys and may consult with counsel, accountants and other skilled Persons to be selected and employed by it, and the Owner Trustee shall not be liable for anything done, suffered or omitted in good faith by it in accordance with the advice or opinion within the scope of such Person's competence of any such counsel, accountants or other skilled Persons and not contrary to this Agreement.

SECTION 6.06. Not Acting in Individual Capacity. Except as provided in this Article VI, in accepting the trusts hereby created the Owner Trustee acts solely as trustee hereunder and not in its individual capacity; and all Persons having any claim against the Owner Trustee by reason of the transactions contemplated by the Transaction Documents shall look only to the Trust Estate (or a part thereof, as the case may be) for payment or satisfaction thereof, except as specifically provided in this Article VI and except to the extent the Owner Trustee shall otherwise agree in any Transaction Document to which it is a party.

ARTICLE VII

INDEMNIFICATION OF THE OWNER TRUSTEE BY THE EQUITY PARTICIPANT

SECTION 7.01. The Equity Participant To Indemnify the Owner Trustee. The Equity Participant agrees to assume liability for, and to indemnify and hold harmless the Owner Trustee and FNB, in its individual capacity, against and from, any and all Claims which may be imposed on, incurred by or asserted at any time against the Owner Trustee (and not indemnified by the Lessee within a reasonable time after demand therefor) in any way relating to or arising out of the Trust Estate, any of the properties included therein, the administration of the Trust Estate or any action or inaction of the Owner Trustee hereunder or under the Transaction Documents, except only that the Equity Participant shall not be required to indemnify the Owner Trustee for Claims arising or resulting from any of the matters described in the last sentences of Sections 5.04 and 6.01. The indemnities contained in this Section 7.01 shall survive the termination of this Agreement.

SECTION 7.02. Compensation and Expenses. The Owner Trustee shall receive as compensation for its services hereunder such ordinary fees as are fair, reasonable and customary for the performance of such services and as may heretofore and from time to time hereafter be agreed upon between the Equity Participant and the Owner Trustee. The Owner Trustee shall be entitled to be reimbursed for its reasonable expenses hereunder and to be compensated reasonably for any extraordinary services rendered hereunder.

ARTICLE VIII

TERMINATION OF TRUST AGREEMENT

SECTION 8.01. Termination of Trust Agreement. This Agreement and the trusts created hereby shall terminate and the Trust Estate shall, subject to the Participation Agreement, the Indenture and Article IV of this Agreement, be distributed to the Equity Participant, and this Agreement shall be of no further force or effect, upon the earlier of (i) the sale or other final disposition by the Owner Trustee of all property constituting part of the Trust Estate and the final distribution by the Owner Trustee of all moneys or other property or proceeds constituting part of the Trust Estate in accordance with the terms of Article IV and (ii) 21 years less one day after the death of the last survivor of all of the descendants living on the date of this Agreement of Joseph P. Kennedy, father of President John F. Kennedy, but if any such rights, privileges or options shall be or become valid under Applicable Law for a period subsequent to the 21st anniversary of the death of such last survivor

(or, without limiting the generality of the foregoing, if legislation shall become effective providing for the validity or permitting the effective grant of such rights, privileges and options for a period in gross exceeding the period for which such rights, privileges and options are hereinabove stated to extend and be valid), then such rights, privileges or options shall not terminate as aforesaid but shall extend to and continue in effect, but only if such nontermination and extension shall then be valid under Applicable Law, until such time as the same shall, under Applicable Law, cease to be valid.

SECTION 8.02. Termination at Option of the Equity Participant. Notwithstanding Section 8.01, this Agreement and the trusts created hereby shall terminate and the Trust Estate shall be distributed to the Equity Participant, and this Agreement shall be of no further force and effect, upon the election of the Equity Participant by notice to the Owner Trustee, if such notice shall be accompanied by the written agreement of the Equity Participant assuming all the obligations of the Owner Trustee under or contemplated by the Transaction Documents and all other obligations of the Owner Trustee incurred by it as trustee hereunder; provided, however, that no such election shall be effective until (i) the lien of the Indenture on the Lease Indenture Estate has been released, (ii) full payment of the principal of and premium, if any, and interest on the Notes has been made and (iii) any lien on the Trust Estate created pursuant to Section 7(b)(4) of the Participation Agreement has terminated. Such written agreement shall be reasonably satisfactory in form and substance to the Owner Trustee and shall release the Owner Trustee from all further obligations of the Owner Trustee hereunder and under the agreements and other instruments mentioned in the preceding sentence.

ARTICLE IX

SUCCESSOR OWNER TRUSTEES, CO-OWNER TRUSTEES AND SEPARATE OWNER TRUSTEES

SECTION 9.01. Resignation of the Owner Trustee; Appointment of Successor. (a) The Owner Trustee may resign at any time without cause by giving at least 30 days' prior written notice to the Equity Participant, the Indenture Trustee and the Lessee, such resignation to be effective on the acceptance of appointment by a successor Owner Trustee under Section 9.01(b). In addition, the Equity Participant may at any time remove the Owner Trustee with or without cause by an instrument in writing delivered to the Owner Trustee, such removal to be effective upon the acceptance of appointment by a successor owner trustee under Section 9.01(b). In case of the resignation or removal of the Owner Trustee, the Equity Participant may appoint a successor Owner Trustee by an instrument signed by the Equity Participant. If

a successor Owner Trustee shall not have been appointed within 30 days after the giving of written notice of such resignation or the delivery of the written instrument with respect to such removal, the Owner Trustee or the Equity Participant may apply to any court of competent jurisdiction to appoint a successor Owner Trustee to act until such time, if any, as a successor shall have been appointed and shall have accepted its appointment as above provided. Any successor Owner Trustee so appointed by such court shall immediately and without further act be superseded by any successor Owner Trustee appointed as above provided within one year from the date of the appointment by such court.

(b) Any successor Owner Trustee, however appointed, shall execute and deliver to the predecessor Owner Trustee an instrument accepting such appointment, and thereupon such successor Owner Trustee, without further act, shall become vested with all the estates, properties, rights, powers, duties and trusts of the predecessor Owner Trustee in the trusts hereunder with like effect as if originally named an Owner Trustee herein; but nevertheless, upon the written request of such successor Owner Trustee, such predecessor Owner Trustee shall execute and deliver an instrument transferring to such successor Owner Trustee, upon the trusts herein expressed, all the estates, properties, rights, powers, duties and trusts of such predecessor Owner Trustee, and such predecessor Owner Trustee shall duly assign, transfer, deliver and pay over to such successor Owner Trustee all moneys or other property then held by such predecessor Owner Trustee upon the trusts herein expressed.

(c) Any successor Owner Trustee, however appointed, shall be a bank or trust company incorporated and doing business within the United States of America and having a combined capital and surplus of at least \$50,000,000, if there be such an institution willing, able and legally qualified to perform the duties of Owner Trustee hereunder upon reasonable or customary terms.

(d) Any corporation into which the Owner 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 Owner Trustee shall be a party, or any corporation to which substantially all the corporate trust business of the Owner Trustee may be transferred, shall, subject to the terms of Section 9.01(c), be the Owner Trustee under this Agreement without further act.

SECTION 9.02. Co-Trustees and Separate Trustees.

Whenever the Owner Trustee or the Equity Participant shall deem it necessary or prudent in order either to conform to any law of any jurisdiction in which all or any part of the Trust Estate shall be situated or to make any claim or bring any suit with respect to the Trust Estate, the Notes or any Transaction Document, or the Owner Trustee or the Equity Participant shall be advised by counsel

satisfactory to it that it is so necessary or prudent, the Owner Trustee and the Equity Participant shall execute and deliver an agreement supplemental hereto and all other instruments and agreements, and shall take all other action, necessary or proper to constitute one or more Persons (and the Owner Trustee may appoint one or more of its officers) either as co-trustee or co-trustees jointly with the Owner Trustee of all or any part of the Trust Estate, or as separate trustee or separate trustees of all or any part of the Trust Estate, and to vest in such Persons, in such capacity, such title to the Trust Estate or any part thereof and such rights or duties as may be necessary or desirable, all for such period and under such terms and conditions as are satisfactory to the Owner Trustee and the Equity Participant. In case any co-trustee or separate trustee shall die, become incapable of acting, resign or be removed, the title to the Trust Estate and all rights and duties of such co-trustee or separate trustee shall, so far as permitted by law, vest in and be exercised by the Owner Trustee, without the appointment of a successor to such co-trustee or separate trustee.

ARTICLE X

SUPPLEMENTS AND AMENDMENTS

SECTION 10.01. Supplements and Amendments. At the written request of the Equity Participant, this Agreement shall be amended by a written instrument signed by the Owner Trustee and the Equity Participant, but if in the opinion of the Owner Trustee any instrument required to be so executed adversely affects any right, duty or liability of, or immunity or indemnity in favor of, it under this Agreement or any of the documents contemplated hereby to which it is a party, or would cause or result in any conflict with or breach of any terms, conditions or provisions of, or default under, its charter documents or by-laws or any document contemplated hereby to which it is a party, the Owner Trustee may in its sole discretion decline to execute such instrument, unless it shall have been provided an indemnity satisfactory to the Owner Trustee by the Equity Participant.

SECTION 10.02. Limitation on Amendments. Notwithstanding Section 10.01, the Owner Trustee shall not execute any amendment which might result in the trusts created hereunder being terminated (i) without the consent of the Indenture Trustee, prior to the release of the lien of the Indenture on the Lease Indenture Estate or prior to the payment in full of the principal of and premium, if any, and interest on the Notes or (ii) without the consent of the holder thereof, prior to the termination of any lien created pursuant to Section 7(b)(4) of the Participation Agreement.

ARTICLE XI

MISCELLANEOUS

SECTION 11.01. No Legal Title to Trust Estate in the Equity Participant. The Equity Participant shall not have legal title to any part of the Trust Estate. No transfer, by operation of law or otherwise, of any right, title or interest of the Equity Participant in and to the Trust Estate or hereunder shall operate to terminate this Agreement or the trusts hereunder or entitle any successor or transferee to an accounting or to the transfer to it of legal title to any part of the Trust Estate.

SECTION 11.02. Sale of Undivided Interest and/or Real Property Interest by the Owner Trustee is Binding. Any sale or other conveyance of the Undivided Interest, the Real Property Interest or any part thereof or any assignment of rights under the Assignment and Assumption by the Owner Trustee made pursuant to the terms of this Agreement or any other Transaction Document shall bind the Equity Participant and shall be effective to transfer and convey all right, title and interest of the Owner Trustee and the Equity Participant in and to the Undivided Interest, the Real Property Interest or any part thereof, or such rights under the Assignment and Assumption, as the case may be. No purchaser or other grantee shall be required to inquire as to the authorization, necessity, expediency or regularity of such sale or conveyance or as to the application of any sale or other proceeds with respect thereto by the Owner Trustee.

SECTION 11.03. Limitations on Rights of Others. Nothing in this Agreement, whether express or implied, shall be construed to give to any Person other than the Owner Trustee and the Equity Participant any legal or equitable right, remedy or claim under or in respect of this Agreement, any covenants, conditions or provisions contained herein or the Trust Estate, all of which are and shall be construed to be for the sole and exclusive benefit of the Owner Trustee and the Equity Participant.

SECTION 11.04. Notices. Unless otherwise expressly specified or permitted by the terms hereof, all notices hereunder shall be given as provided in the Participation Agreement.

SECTION 11.05. Severability. Any provision of this Agreement which is prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and any such prohibition or unenforceability in any jurisdiction shall not invalidate or render unenforceable such provision in any other jurisdiction.

SECTION 11.06. Limitation on the Equity Participant's Liability. The Equity Participant shall not have any liability for the performance of this Agreement except as expressly set forth herein.

SECTION 11.07. Separate Counterparts. This Agreement may be executed by the parties hereto in separate counterparts, each of which when so executed and delivered shall be an original, but all such counterparts shall together constitute but one and the same instrument.

SECTION 11.08. Successors and Assigns. All covenants and agreements contained herein shall be binding upon, and inure to the benefit of, the Owner Trustee and its successors and assigns and the Equity Participant and its successors and assigns, all as herein provided. Any request, notice, direction, consent, waiver or other instrument or action by the Equity Participant shall bind the successors and assigns of the Equity Participant.

SECTION 11.09. Transfer of Interests. Subject to the provisions of Section 15 of the Participation Agreement, the Equity Participant may assign, convey or otherwise transfer all or any part of its right, title and interest in and to this Agreement and the Trust Estate. In case of any such assignment, conveyance or transfer of less than all of the interest of the Equity Participant, (i) the transferor and transferee or transferees shall be severally obligated with respect to the indemnification obligations imposed under Section 7.01 in accordance with the interest held by each of them and (ii) appropriate amendments shall be made to this Agreement to provide for the situation in which there is more than one Equity Participant as may be agreed to by the transferor and transferee or transferees and consented to by the Owner Trustee. No such assignment, conveyance or transfer shall violate any provision of Applicable Law or create a relationship which would be in violation thereof. The Owner Trustee shall not be on notice of or otherwise be bound by any such assignment, conveyance or transfer until it shall have received an executed counterpart of the instrument of such assignment, conveyance or transfer.

SECTION 11.10. Headings. The headings of the various Articles and Sections herein are for convenience of reference only and shall not define or limit any of the terms or provisions hereof.

SECTION 11.11. Governing Law. This Agreement shall in all respects be governed by, and construed in accordance with, the laws of the State of New York, including all matters of construction, validity and performance, except to the extent that, pursuant to the laws of the State of Arizona, the laws of such State are mandatorily applicable hereto.

SECTION 11.12. Administration of Trust. The principal place of administration of the Trust shall be in Boston, Massachusetts.

SECTION 11.13. Performance by the Equity Participant. Any obligation of the Owner Trustee hereunder or under any Transaction Document or other document contemplated herein may be performed by the Equity Participant and any such performance shall not be construed as a revocation of the trusts created hereby.

SECTION 11.14. Conflict with Transaction Documents. If this Agreement (or any instructions given by the Equity Participant pursuant hereto) shall require that any action be taken with respect to any matter and any other Transaction Document (or any instructions duly given in accordance with the terms thereof) shall require that a different action be taken with respect to such matter, and such actions shall be mutually exclusive, the provisions of such other Transaction Document, in respect thereof, shall control.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective officers thereunto duly authorized, as of the day and year first above written.

SECURITY PACIFIC CAPITAL LEASING
CORPORATION

By:



Senior Vice President

THE FIRST NATIONAL BANK OF BOSTON,

By:

Assistant Vice President

SECTION 11.12. Administration of Trust. The principal place of administration of the Trust shall be in Boston, Massachusetts.

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SECTION 11.14. Conflict with Transaction Documents. If this Agreement (or any instructions given by the Equity Participant pursuant hereto) shall require that any action be taken with respect to any matter and any other Transaction Document (or any instructions duly given in accordance with the terms thereof) shall require that a different action be taken with respect to such matter, and such actions shall be mutually exclusive, the provisions of such other Transaction Document, in respect thereof, shall control.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective officers thereunto duly authorized, as of the day and year first above written.

SECURITY PACIFIC CAPITAL LEASING
CORPORATION

By: _____
Senior Vice President

THE FIRST NATIONAL BANK OF BOSTON,

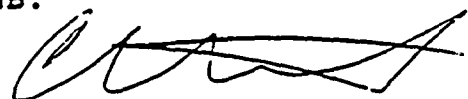
By: _____
Assistant Vice President

SECTION 15.6.1
LESSOR'S CERTIFICATE
APS Unit 2/1986-1

The undersigned, being a duly elected, qualified and acting Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association (FNB), hereby certifies, for and on behalf of FNB, as follows:

1. Reference is made to (i) the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, as amended (the ANPP Participation Agreement), and (ii) the sale and leaseback transaction proposed to be entered into by Arizona Public Service Company (APS) on or before August 20, 1986, with respect to Palo Verde Nuclear Generating Station (PVNGS) Unit 2 and APS's interest therein (the Proposed APS Sale and Leaseback Transaction);
2. In connection with the Proposed APS Sale and Leaseback Transaction, FNB will enter into a Trust Agreement (the Trust Agreement) with an affiliate of Security Pacific Corporation constituting FNB the trustee (in such capacity, Owner Trustee) of a grantor trust (the Grantor Trust); thereafter, the Grantor Trust will acquire from APS an undivided ownership interest of up to approximately 4.2% in certain assets constituting part of PVNGS Unit 2 and up to approximately 1.4% of the PVNGS site and lease back such interest to APS pursuant to a Facility Lease having a primary term of at least 25 years; and
3. Upon the execution and delivery of the Trust Agreement and upon consummation of the Proposed APS Sale and Leaseback Transaction, FNB, solely in its capacity as Owner Trustee and not otherwise, confirms that, except as provided in Sections 15.2.2, 15.6.4 and 15.10 of the ANPP Participation Agreement, APS shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Grantor Trust and any mortgagee, trustee and secured party of the Grantor Trust of the type described in Section 15.1.2 of the ANPP Participation Agreement) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of APS transferred to the Grantor Trust pursuant to the Proposed APS Sale and Leaseback Transaction.

WITNESS the signature of the undersigned this 8th day of August, 1986, for and on behalf of FNB.



Clark M. Whitcomb
Vice President

CERTAIN RIGHTS OF THE LESSOR UNDER THIS FACILITY LEASE HAVE BEEN ASSIGNED TO, AND ARE SUBJECT TO A SECURITY INTEREST IN FAVOR OF, CHEMICAL BANK, AS INDENTURE TRUSTEE UNDER A TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE, DATED AS OF AUGUST 1, 1986. THIS FACILITY LEASE HAS BEEN EXECUTED IN SEVERAL COUNTERPARTS. SEE SECTION 22(e) OF THIS FACILITY LEASE FOR INFORMATION CONCERNING THE RIGHTS OF HOLDERS OF VARIOUS COUNTERPARTS HEREOF.

THIS COUNTERPART IS NOT THE ORIGINAL COUNTERPART..

FACILITY LEASE

dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity,
but solely as Owner Trustee
under a Trust Agreement, dated as of August 1, 1986,
with Security Pacific Capital Leasing Corporation

Lessor

and

ARIZONA PUBLIC SERVICE COMPANY

Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2
Security Pacific Capital Leasing Corporation

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FACILITY LEASE

THIS FACILITY LEASE, dated as of August 1, 1986 between THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement, dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation, as Lessor (the Lessor), and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, as Lessee (the Lessee).

W I T N E S S E T H :

WHEREAS, the Lessor owns the Undivided Interest and the Real Property Interest; and

WHEREAS, the Lessee desires to lease the Undivided Interest from the Lessor, and the Lessor is willing to lease the Undivided Interest and the Real Property Interest to the Lessee, all on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A hereto. References in this Facility Lease to sections, paragraphs and clauses are to sections, paragraphs and clauses in this Facility Lease unless otherwise indicated.

SECTION 2. Lease of Undivided Interest; Term; Personal Property.

(a) Lease of Undivided Interest. Upon the terms and subject to the conditions of this Facility Lease, the Lessor hereby leases to the Lessee, and the Lessee hereby leases from the Lessor, the Undivided Interest.

(b) Term. The term of this Facility Lease shall begin August 18, 1986, and shall end on the last day of the Lease Term.

(c) Personal Property. It is the express intention of the Lessor and the Lessee that title to the Undivided Interest and every portion thereof is severed, and shall be and remain severed, from title to the real estate constituting the Real Property Interest and the PVNGS Site. The Lessor and the Lessee intend that the Undivided Interest shall constitute personal property to the maximum extent permitted by Applicable Law.

(d) Description. The Undivided Interest is described on Schedule 6 hereto. The Real Property Interest is described on Schedule 7 hereto.

SECTION 3. Rent; Adjustments to Rent..

(a) Basic Rent. The Lessee shall pay to the Lessor, as basic rent (herein referred to as Basic Rent) for the Undivided Interest, the following amounts:

(i) on December 30, 1986, an amount equal to the daily equivalent of Basic Rent (set forth in Schedule 1 hereto) plus or minus any Rent Differential for the period from the Closing Date to and including December 31, 1986;

(ii) on June 30, 1987 and on each Basic Rent Payment Date thereafter to and including December 30, 2015, an amount equal to the percentage of Facility Cost set forth opposite such Basic Rent Payment Date in Schedule 1 hereto, plus or minus any Rent Differential;

(iii) if the Lessee shall elect the Fixed Rate Renewal Term, on June 30, 2016 and on each Basic Rent Payment Date thereafter during

the Fixed Rate Renewal Term, an amount equal to one-half of an amount determined by dividing an amount equal to the amount of all payments of Basic Rent payable with respect to the Basic Lease Term pursuant to clause (ii) of this Section 3(a) (taking into account the amount of any Rent Differential and any adjustments pursuant to Sections 3(d) and 3(e)), by 58; and

(iv) if the Lessee shall elect a Fair Market Renewal Term, on the first Basic Rent Payment Date in the Fair Market Renewal Term and on each Basic Rent Payment Date thereafter during the Fair Market Renewal Term, an amount equal to the greater of (A) the Fair Market Rental Value of the Undivided Interest and (B) the amount payable on each Basic Rent Payment Date during the Fixed Rate Renewal Term as determined pursuant to clause (iii) of this Section 3(a).

Payments made on December 30, 1986 and on each Basic Rent Payment Date shall be in satisfaction of the Lessee's obligation to pay Basic Rent for the six-month period ending on the last day of the month in which such Rent Payment Date shall have occurred (or the period commencing with the Closing Date and ending on December 31, 1986, in the case of the payment made on December 30, 1986). If an interest payment on any Note shall be due on a date other than December 30, 1986 or a Basic Rent Payment Date and the amount thereof is not included in a Refunding Loan being made on such date, the Lessee shall pay Basic Rent on such date equal to such interest payment and such payment of Basic Rent shall be credited against the Basic Rent due on December 30, 1986 or the Basic Rent Payment Date next succeeding the date that such additional Basic Rent shall have been paid.

(b) Supplemental Rent. The Lessee shall pay the following amounts (herein referred to as Supplemental Rent):

(i) when due or, where no due date is specified, on demand, any amount (other than Basic Rent, Casualty Value, Extraordinary Casualty Value and Special Casualty Value) which the Lessee assumes the obligation to pay

or agrees to pay to the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee or any Indemnatee under this Facility Lease, any other Transaction Document or any Collateral Trust Indenture and an amount equal to any amount which the Lessor is obligated to pay under Sections 6.9, 7.6 or 8.7 of the Indenture or under the Initial Series Notes other than principal and interest;

(ii) when due any amount payable hereunder as Casualty Value, Extraordinary Casualty Value or Special Casualty Value, and an amount equal to any premium or prepayment penalty with respect to the Notes;

(iii) on demand and in any event on the Basic Rent Payment Date next succeeding the date such amounts shall be due and payable hereunder, to the extent permitted by Applicable Law, interest (computed on the same basis as interest on the Notes is computed) at a rate per annum equal to (A) the Overdue Interest Rate, on that portion of the payment of Basic Rent or Supplemental Rent distributable pursuant to clause "first" of Section 5.1 or clause "second" of Section 5.3 of the Indenture (determined prior to the computation of interest on overdue payments referred to in such clauses), and (B) the Penalty Rate, on the balance of any such payment of Basic Rent or Supplemental Rent (including, without limitation, to the extent permitted by Applicable Law, interest payable pursuant to this clause (iii)) not paid when due (without regard to any period of grace) for any period for which the same shall be overdue.

The Lessor shall have all rights, powers and remedies provided for in this Facility Lease, at law, in equity or otherwise, in the case of non-payment of Basic Rent or Supplemental Rent. Drawings under the Letter of Credit shall be deemed to be in satisfaction of the Lessee's obligation to pay the Equity Portion of Rent hereunder to the extent of such drawing.

(c) Form of Payment. Subject to Section 11(b); each payment of Rent under this Facility Lease shall be made in immediately available funds no later than 12:00 noon, local time at the place of receipt, on the date each such payment shall be due and payable hereunder and shall be paid either (A) in the case of payments other than Excepted Payments, to the Lessor at its address determined in accordance with Section 17, or at such other address as the Lessor may direct by notice in writing to the Lessee, or (B) in the case of Excepted Payments, to such Person as shall be entitled to receive such payment at such address as such Person may direct by notice in writing to the Lessee. If the date on which any payment of Rent is due hereunder shall not be a Business Day, the payment otherwise due thereon shall be due and payable on the preceding Business Day, with the same force and effect as if paid on the nominal date provided in this Facility Lease.

(d) Adjustments to Rent for Change in Tax Law. Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values attached hereto shall be adjusted (upward or downward) to preserve Net Economic Return if there is any change in the Code or successor legislation adopted by the Ninety-ninth Congress and enacted into law (including technical corrections thereof and proposed, temporary or final regulations resulting therefrom) other than a change in respect of an "alternative minimum tax" (including any "add-on minimum tax having the same economic effect as an "alternative minimum tax"), and if H.R. 3838 is not adopted by the Ninety-ninth Congress, changes in Federal income tax rates are adopted by the One Hundredth Congress and enacted into law (herein referred to as a Change in Tax Law). Any adjustment under this Section 3(d) shall be made no more frequently than annually.

For purposes of determining whether a statutory or regulatory change constitutes a Change in Tax Law requiring adjustment pursuant to Section 3(d) and determining the effect thereof for purposes of making any adjustments required thereunder, the original Equity Participant shall be deemed to be the Equity Participant notwithstanding any transfer of its interest as such (whether or not permitted by Section 15 of the Participation Agreement); provided, however, that a successor Equity Participant shall be treated as the

Equity Participant for such purposes if the transfer to such successor Equity Participant was permitted by Section 15 of the Participation Agreement and if both the original Equity Participant and such successor Equity Participant are members of the same affiliated group of corporations that files a consolidated return for Federal income tax purposes.

(e) Adjustments to Rent for Changes in Pricing Assumptions. Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values attached hereto shall be adjusted (upward or downward) to preserve Net Economic Return if there is any change in the Pricing Assumptions. Any adjustments pursuant to Section 3(d) or this Section 3(e) hereof also (i) shall satisfy the provisions of Revenue Procedure 75-21, Revenue Procedure 75-28, and any other applicable statutes, regulations, revenue procedures, revenue rulings or technical information releases relating to the subject matter of such revenue procedures, shall be made in a manner designed to avoid application of Section 467(b)(2) of the Code and any regulations thereunder or any other similar provision of Federal income tax law and otherwise shall not cause any adverse effect under any Federal income tax laws in effect at the time of such adjustment, (ii) shall not cause any adverse effect under current accounting standards for leveraged leases as provided in Statement of Financial Accounting Standards No. 13 and (iii) shall, to the extent possible and not inconsistent with the foregoing, minimize the net present value cost of the Basic Rent to the Lessee to the extent that the foregoing criteria are met.

(f) Computation of Adjustments. As soon as practicable after the occurrence of an event requiring an adjustment to Basic Rent, and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values attached hereto, pursuant to Sections 3(d) or (e), the Equity Participant shall make the necessary computations and furnish to the Lessee, any Loan Participant, the Lessor, the Indenture Trustee and any Collateral Trust Trustee the revised amounts and percentages (together with a certificate of the chief financial or other appropriate officer of the Equity Participant to the effect that such revised amounts and percentages comply with the method for adjustment described in such Sections), which amounts and percentages shall be

implemented upon the later of (i) delivery of such amounts and percentages and (ii) if the Letter of Credit is in effect, 30 days after the delivery thereof, and, in either case, effective as of the later of (y) the date of occurrence of the event requiring such adjustment or (z) if the Letter of Credit is in effect, the date on which notice of such adjustment is given to the bank which has issued the Letter of Credit (taking into account any payment of Basic Rent already made) and shall remain effective until changed in consequence of any verification procedure set forth below. Such revised amounts and percentages shall be subject to verification (at the Lessee's request) by the Equity Participant's nationally recognized independent public accountants, in which case such accountants shall either (i) confirm to the Lessee in writing that such revised amounts were computed on a basis consistent with the original calculations, or (ii) compute and provide to the Lessee, the Lessor, the Equity Participant, each Loan Participant, the Indenture Trustee and any Collateral Trust Trustee revised amounts and percentages which are on such a basis. The revised amounts and percentages, as so confirmed or computed if applicable, shall be conclusive and binding upon the Lessee, the Lessor, the Equity Participant, each Loan Participant and the Indenture Trustee. The cost of any such verification shall be borne by the Lessee, unless such accountants shall require a downward adjustment to the revised amounts and percentages originally provided by the Equity Participant which is greater than 10% of the amount of the adjustment to Basic Rent so provided, in which case such cost shall be paid by the Equity Participant. Each adjustment pursuant to Section 3(d) or 3(e) may, but need not, be evidenced by the execution and delivery of a supplement to this Facility Lease in form and substance satisfactory to the Lessee and the Equity Participant, but shall be effective as provided herein without regard to the date on which such supplement to this Facility Lease is so executed and delivered.

(g) Sufficiency of Basic Rent and Supplemental Rent. Notwithstanding any other provision of this Facility Lease or any other Transaction Document, (i) the amount of Basic Rent payable on December 30, 1986 and on each Basic Rent Payment Date during the Basic Lease Term shall be at least equal to the aggregate amount of principal, premium, if any, and accrued interest then payable (or payable on or before the last

day of the month in which such Basic Rent Payment Date shall have occurred) on all Notes then Outstanding and (ii) each payment of Casualty Value, Extraordinary Casualty Value and Special Casualty Value shall in no event be less (when added to all other amounts required to be paid by the Lessee under this Facility Lease in respect of any Event of Loss or Deemed Loss Event or termination of this Facility Lease) than an amount sufficient, as of the date of payment, to pay in full the principal of, and premium, if any, and interest on all Notes Outstanding on and as of such date of payment (taking into account any assumption of the Notes by the Lessee on the date such payment is due).

(h) Rent Differential. So long as any series of Notes shall be Outstanding which bears interest at a floating rate, each installment of Basic Rent payable on December 30, 1986 or a Basic Rent Payment Date shall be increased or decreased, as the case may be, by the Rent Differential. For purposes hereof, "Rent Differential" shall mean, as of December 30, 1986 or any Basic Rent Payment Date, the difference between (i) the aggregate amount of interest due and payable on the Notes on December 30, 1986 and on each Basic Rent Payment Date and (ii) the aggregate amount of interest indicated on Schedule 8 hereto for such date. If, as of December 30, 1986 or any Basic Rent Payment Date, (A) the amount determined in accordance with clause (i) of the immediately preceding sentence shall exceed the amount determined in accordance with clause (ii) of such sentence, the amount of Basic Rent due on such date shall be increased by the Rent Differential, and (B) the amount determined in accordance with such clause (ii) shall exceed the amount determined in accordance with such clause (i), the amount of Basic Rent due on such date shall be decreased by the Rent Differential.

(i) Lessee as Agent. Unless and until an Event of Default has occurred and been continuing hereunder, the Lessor hereby appoints the Lessee as its agent with respect to all matters relating to the election of interest rates and options with respect thereto under the Initial Series Notes.

SECTION 4. Net Lease.

This Facility Lease (as originally executed and as modified, supplemented and amended from time to time) is a net lease and the Lessee hereby acknowledges and agrees that the Lessee's obligation to pay all Rent hereunder, and the rights of the Lessor in and to such Rent, shall be absolute, unconditional and irrevocable and shall not be affected by any circumstances of any character, including, without limitation, (i) any set-off, abatement, counterclaim, suspension, recoupment, reduction, defense or other right or claim which the Lessee may have against the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp, the Operating Agent, any ANPP Participant, any vendor or manufacturer of any equipment or assets included in the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site, PVNGS, or any part of any thereof, or any other Person for any reason whatsoever, (ii) any defect in or failure of the title, merchantability, condition, design, compliance with specifications, operation or fitness for use of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, (iii) any destruction of, damage to, or removal, abandonment, shutdown, salvage, scrapping, requisition, taking, loss, theft or destruction of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, or any interference, interruption or cessation in the use or possession thereof or of the Undivided Interest by the Lessee or by any other Person (including, without limitation, the Operating Agent or any other ANPP Participant) for any reason whatsoever or of whatever duration, (iv) any restriction, prevention or curtailment of or interference with any use of all or any part of the Undivided Interest, Unit 2, any Capital Improvement, the Real Property Interest, the PVNGS Site or PVNGS, (v) any insolvency, bankruptcy, reorganization or similar proceeding by or against the Lessee, the Lessor, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp, the Operating Agent, any other ANPP Participant or any other Person, (vi) the invalidity, illegality or unenforceability of this Facility Lease, any other Transaction Document, any Financing Document, the ANPP

Participation Agreement or any other instrument referred to herein or therein or any other infirmity herein or therein or any lack of right, power or authority of the Lessor, the Lessee, the Equity Participant, the Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp or any other Person to enter into this Facility Lease, any other Transaction Document or any Financing Document, or any doctrine of force majeure, impossibility, frustration, failure of consideration, or any similar legal or equitable doctrine that the Lessee's obligation to pay Rent is excused because the Lessee has not received or will not receive the benefit for which the Lessee bargained, it being the intent of the Lessee to assume all risks from all causes whatsoever that the Lessee does not receive such benefit, (vii) the breach or failure of any warranty or representation made in this Facility Lease or any other Transaction Document or any Financing Document by the Lessor, the Equity Participant, Indenture Trustee, any Collateral Trust Trustee, the Original Loan Participants, any Loan Participant, Funding Corp or any other Person, (viii) any amendment or other change of, or any assignment of rights under, this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, or any waiver, action or inaction under or in respect of this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, or any exercise or non-exercise of any right or remedy under this Facility Lease, any other Transaction Document, any Financing Document or any ANPP Project Agreement, including, without limitation, the exercise of any foreclosure or other remedy under the Indenture, any Collateral Trust Indenture or this Facility Lease, or the sale of Unit 2, any Capital Improvement, the Undivided Interest, the Real Property Interest, the PVNGS Site or PVNGS, or any part thereof or any interest therein, or (ix) any other circumstance or happening whatsoever whether or not similar to any of the foregoing. The Lessee acknowledges that, by conveying the leasehold estate created by this Facility Lease to the Lessee and by putting the Lessee in possession of the Undivided Interest and the Real Property Interest, the Lessor has performed all of the Lessor's obligations under and in respect of this Facility Lease, except the covenant contained in Section 6(a). The Lessee hereby waives, to the extent permitted by Applicable Law, any and all rights which it may now have or which at any time hereafter may be

conferred upon it, by statute or otherwise, to terminate, cancel, quit or surrender this Facility Lease or to effect or claim any diminution or reduction of Rent payable by the Lessee hereunder, including, without limitation, the provisions of Arizona Revised Statutes Section 33-343, except in accordance with the express terms hereof. If for any reason whatsoever this Facility Lease shall be terminated in whole or in part by operation of law or otherwise, except as specifically provided herein, the Lessee nonetheless agrees to pay to the Lessor or other Person entitled thereto an amount equal to each installment of Basic Rent and all Supplemental Rent at the time such payment would have become due and payable in accordance with the terms hereof had this Facility Lease not been terminated in whole or in part. Each payment of Rent made by the Lessee hereunder shall be final and the Lessee shall not seek or have any right to recover all or any part of such payment from the Lessor or any other Person for any reason whatsoever. All covenants, agreements and undertakings of the Lessee herein shall be performed at its cost, expense and risk unless expressly otherwise stated. Nothing in this Section 4 or elsewhere shall be construed as a guaranty by the Lessee of any residual value in the Undivided Interest or the Real Property Interest or as a guaranty of the Notes or any Bonds. Any provision of Section 7(b)(2) or 8(c) of the Participation Agreement to the contrary notwithstanding, if the Lessee shall fail to make any payment of Rent to any Person when and as due (taking into account applicable grace periods), such Person shall have the right at all times, to the exclusion of the ANPP Participants, to demand, collect, sue for, enforce obligations relating to and otherwise obtain all amounts due in respect of such Rent.

SECTION 5. Return of the Undivided Interest; Disposition Services.

(a) Return of the Undivided Interest. Unless the Lessee has acquired the Undivided Interest as provided herein, on the Lease Termination Date, the Lessee will surrender possession of the Undivided Interest to the Lessor (or to a Person specified by the Lessor to the Lessee in writing not less than 6 months prior to the Lease Termination Date) with full rights as a "Transferee" and the sole "Participant" with respect to the Undivided Interest within the meaning of Section 15.10 of the ANPP Participation Agreement, and will

furnish to the Lessor: (i) copies certified by a senior officer of the Lessee of all Governmental Actions necessary to effect such surrender (including, without limitation, appropriate amendments to the License permitting the Lessor (without being required to change its business or corporate structure) and for such Person to possess the Undivided Interest without the continued involvement of the Lessee), which Governmental Action shall be in full force and effect and not subject to any judicial or administrative contest, challenge or review; (ii) if not previously executed and delivered by the Lessee, and if desired by the Lessor, a ground lease covering that portion of the PVNGS Site which is included in the Real Property Interest, which ground lease shall have a term ending on the date of reversion of the Real Property Interest and shall be otherwise reasonably satisfactory to the Lessor in replacement for the Real Property Interest; and (iii) an opinion of counsel (which may be Mudge Rose Guthrie Alexander & Ferdon, Snell & Wilmer or other counsel experienced in matters pertaining to the Governmental Actions required, reasonably satisfactory to the Equity Participant) to the effect that (A) the Lessee has obtained all Governmental Actions and actions under the ANPP Participation Agreement necessary to effect such surrender by the Lessee and receipt of possession by the Lessor (or to the Person so specified by the Lessor) of the Undivided Interest and the Real Property Interest, (B) the Lessor (or the Person specified by the Lessor) is a NRC Licensee and an ANPP Participant (with all rights and obligations attendant thereto) and no additional Governmental Action will be required in connection with the possession by the Lessor (or the Person specified by the Lessor) of the Undivided Interest and the Real Property Interest, (C) such Governmental Action is in full force and effect and not subject to any judicial or administrative contest, challenge or review and (D) to the extent the aforementioned ground lease is required, such ground lease (1) has been duly authorized, executed and delivered, (2) constitutes the legal, valid and binding obligation of the Lessee, (3) does not require the consent of any Person or such consent has been previously received and (4) is not inconsistent with any ANPP Project Agreement. At the time of such return the Lessee shall pay or have paid all amounts due and payable, or to become due and payable, by it as an ANPP Participant under each and every ANPP Project Agreement allocable or chargeable (whether or not payable during or after the Lease Term) to the

Undivided Interest in respect of any period or periods ending on or prior to the Lease Termination Date (including, without limitation, all amounts payable with respect to any and all Capital Improvements to Unit 2 or the PVNGS Site approved or authorized (without the concurrence of the Equity Participant) prior to the end of the Lease Term, whether or not implementation thereof has been completed on or prior to the Lease Termination Date); and the Undivided Interest shall be free and clear of all Liens (other than Permitted Liens described in clauses (i), (v) (other than those for which satisfactory arrangements for the payment thereof have been made and those arising by, through or under the Lessee alone), (vi), (vii) (other than those arising by, through, or under the Lessee alone), (ix) or (x) of the definition of such term) and in the condition and state of repair required by Section 8. In the event that on or prior to the Lease Termination Date there shall have occurred a default by any ANPP Participant (other than the Lessee) under the ANPP Participation Agreement and such default shall not have been cured by the defaulting ANPP Participant, then (x) the Lessee agrees to indemnify and hold the Lessor (and each successor, assign and transferee thereof) harmless against any and all obligations under the ANPP Participation Agreement with respect to contributions or payments required to be made thereby as a result of such default and (y) the Lessor (and each successor, assign and transferee thereof) agrees to reimburse the Lessee for all amounts paid by the Lessee pursuant to the foregoing clause (x) in respect of the period following the Lease Termination Date to the extent, but only to the extent, that the Lessor (or such successor, assign or transferee) shall have actually received net proceeds from the sale of the Generation Entitlement Share of the defaulting ANPP Participant as a result of the payment made by the Lessee pursuant to the foregoing clause (x), and, to the extent the Lessor (or such successor, assign or transferee) shall have received such proceeds, the amount to be reimbursed to the Lessee pursuant to this clause (ii) shall include interest at the Prime Rate from the date of any payment by the Lessee pursuant to the foregoing clause (i) through the date of reimbursement of such amount pursuant to this clause (ii).

(b) **Disposition Services.** The Lessee agrees that if it does not exercise its option to renew or purchase as provided in Sections 12 and 13, respectively, then during the last thirty-six months of

the Lease Term, the Lessee will fully cooperate with the Lessor in connection with the Lessor's efforts to lease or dispose of the Undivided Interest and the Real Property Interest, including using the Lessee's reasonable efforts to lease or dispose of the Undivided Interest and the Real Property Interest. The Lessor agrees to reimburse the Lessee for reasonable out-of-pocket costs and expenses of the Lessee incurred at the request of the Lessor or the Equity Participant in connection with such cooperation and such efforts, but only to the extent of proceeds actually received by the Lessor.

SECTION 6. Warranty of the Lessor.

(a) Quiet Enjoyment. The Lessor warrants that until the Lease Termination Date, if the Lessee is in compliance with each and every material term and provision of this Facility Lease and each other Transaction Document to be complied with by the Lessee, the Lessee's use and possession of Unit 2, including the Undivided Interest, shall not be interrupted by the Lessor or any Person claiming by, through or under the Lessor, and their respective successors and assigns.

(b) Disclaimer of Other Warranties. The warranty set forth in Section 6(a) is in lieu of all other warranties of the Lessor or the Equity Participant, whether written, oral or implied, with respect to this Facility Lease, Unit 2, any Capital Improvement, the Real Property Interest, PVNGS or the PVNGS Site. As among the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, the Indenture Trustee, any Collateral Trust Trustee, the Lessor and the Lessee, execution by the Lessee of this Facility Lease shall be conclusive proof of the compliance of Unit 2 (including any Capital Improvement), the Undivided Interest and the Real Property Interest with all requirements of this Facility Lease, and the Lessee acknowledges and agrees that (i) NEITHER THE LESSOR NOR THE EQUITY PARTICIPANT IS A MANUFACTURER OR A DEALER IN PROPERTY OF SUCH KIND AND (ii) THE LESSOR LEASES AND THE LESSEE TAKES THE UNDIVIDED INTEREST AND THE REAL PROPERTY INTEREST, AND SHALL TAKE EACH CAPITAL IMPROVEMENT, AND ANY PART THEREOF, AS IS AND WHERE IS WITH ALL FAULTS, and, until such time as the Indenture is discharged, subject to the lien of the Indenture Trustee, and neither the Lessor nor the Equity Participant shall be deemed to have made, and THE LESSOR

AND THE OWNER PARTICIPANT EACH HEREBY DISCLAIMS AND NEITHER THE LESSOR NOR THE EQUITY PARTICIPANT SHALL HAVE ANY DUTIES WITH RESPECT TO, ANY OTHER REPRESENTATION OR WARRANTY, EITHER EXPRESS OR IMPLIED, AS TO ANY MATTER WHATSOEVER, INCLUDING, WITHOUT LIMITATION, THE DESIGN OR CONDITION OF UNIT 2, ANY CAPITAL IMPROVEMENT, THE UNDIVIDED INTEREST, THE PVNGS SITE OR PVNGS, OR ANY PART THEREOF, THE MERCHANTABILITY THEREOF OR THE FITNESS THEREOF FOR ANY PARTICULAR PURPOSE, TITLE TO UNIT 2, ANY CAPITAL IMPROVEMENT, THE UNDIVIDED INTEREST, THE REAL PROPERTY INTEREST, THE PVNGS SITE OR PVNGS, OR ANY PART THEREOF, THE QUALITY OF THE MATERIAL OR WORKMANSHIP THEREOF OR CONFORMITY THEREOF TO SPECIFICATIONS, FREEDOM FROM PATENT OR TRADEMARK INFRINGEMENT OR THE ABSENCE OF ANY LATENT OR OTHER DEFECTS, WHETHER OR NOT DISCOVERABLE, NOR SHALL THE LESSOR OR THE OWNER PARTICIPANT BE LIABLE FOR INCIDENTAL OR CONSEQUENTIAL DAMAGES (INCLUDING LIABILITY IN TORT, STRICT, ABSOLUTE OR OTHERWISE), it being agreed that all such risks, as among the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, any Collateral Trust Trustee, the Indenture Trustee, the Lessor and the Lessee, are to be borne by the Lessee. The provisions of this Section 6(b) have been negotiated, and, except to the extent otherwise expressly provided in Section 6(a), the foregoing provisions are intended to be a complete exclusion and negation of any representations or warranties by the Lessor, the Equity Participant, the Original Loan Participants, any Loan Participant, Funding Corp, any Collateral Trust Trustee or the Indenture Trustee, express or implied, with respect to Unit 2 (including any Capital Improvement), the Undivided Interest, the Real Property Interest, PVNGS or the PVNGS Site that may arise pursuant to any law now or hereafter in effect, or otherwise.

(c) Enforcement of Certain Warranties. The Lessor authorizes the Lessee (directly or through agents, including the Operating Agent), at the Lessee's expense, to assert for the Lessor's account, during the Lease Term, all of the Lessor's rights (if any) under any applicable warranty and any other claims (under this Facility Lease or any Purchase Document) that the Lessee or the Lessor may have against any vendor or manufacturer with respect to Unit 2 (including any Capital Improvement) or the Undivided Interest, and the Lessor agrees to cooperate, at the Lessee's expense, with the Lessee and the Operating Agent in asserting such rights. Any amount receivable (without regard to any

right of setoff or other similar right of any Person against the Lessee) by the Lessee as payment under any such warranty or other claim against any vendor or manufacturer (or, if such warranty or claim relates to the Undivided Interest or the Retained Assets, the portion of such received amount appropriately allocable to the Undivided Interest) shall be applied in accordance with Sections 9(g), (h) and (i).

SECTION 7. Liens.

The Lessee will not directly or indirectly create, incur, assume or permit to exist any Lien except Permitted Liens on or with respect to the Undivided Interest, the Real Property Interest, the Lessor's title thereto or any interest of the Lessor or Lessee therein (and the Lessee will promptly, at its own expense, take such action as may be necessary duly to discharge any such Lien, except Permitted Liens).

SECTION 8. Operation and Maintenance; Capital Improvements.

(a) Operation and Maintenance. The Lessee agrees that (A) Unit 2 will be maintained in such condition that Unit 2 will have the capacity and functional ability to perform, on a continuing basis (ordinary wear and tear excepted), in normal commercial operation, the functions and substantially at the ratings for which it was designed, (B) Unit 2 will be operated, serviced, maintained and repaired, and all necessary or useful parts and components thereof will be replaced, so that the condition and operating efficiency will be maintained and preserved, ordinary wear and tear excepted, in all material respects in accordance with (1) Prudent Utility Practice for items of similar size and nature, (2) such operating standards as shall be required to take advantage of and enforce all available warranties, (3) the terms and conditions of all insurance policies maintained in effect at any time with respect thereto and (4) the terms of the ANPP Participation Agreement, (C) Unit 2 will be used, possessed, operated and maintained in compliance with all material applicable Governmental Actions (including the License) affecting PVNGS or Unit 2 or the use, possession, operation and maintenance thereof and (C) the Lessee will otherwise act in accordance with the standards set forth in the ANPP Participation Agreement. The Lessee will comply with all its obligations under Applicable Law affecting

Unit 2, the Undivided Interest, PVNGS, the Real Property Interest and the PVNGS Site, and the use, operation and maintenance thereof. The Lessee agrees to (i) exercise its rights under the ANPP Participation Agreement so that there will always be an Operating Agent under the ANPP Participation Agreement and (ii) maintain in full force and effect a license from the NRC adequate for it to possess the Undivided Interest and the Real Property Interest, in each case under the circumstances contemplated by the ANPP Participation Agreement. The Lessee will keep and maintain proper books and records (i) relating to all Operating Funds (as defined in the ANPP Participation Agreement) provided by it to the Operating Agent under the ANPP Participation Agreement and (ii) relating to the application of such Operating Funds to the operation and maintenance of Unit 2 and the acquisition, construction and installation of Capital Improvements (upon receipt of the requisite information from the Operating Agent), all in accordance with the Uniform System of Accounts. The Lessor shall not be obliged in any way to maintain, alter, repair, rebuild or replace Unit 2, any Capital Improvement, the Undivided Interest or the Real Property Interest, or any part thereof, or, except as provided in Section 8(f), to pay the cost of alteration, rebuilding, replacement, repair or maintenance of Unit 2, any Capital Improvement, the Undivided Interest or the Real Property Interest, or any part thereof, and the Lessee expressly waives the right to perform any such action at the expense of the Lessor pursuant to any law at any time in effect.

(b) Inspection. The Lessor, the Equity Participant, the Indenture Trustee and any Collateral Trust Trustee shall have the right to inspect Unit 2 and the Retained Assets (subject, in each event, to the ANPP Participation Agreement, Applicable Law and applicable confidentiality undertakings and procedures established by the Operating Agent) at their expense. The Lessor and the Equity Participant shall have the right to inspect, at their expense, the books and records of the Lessee relating to PVNGS, and make copies of and extracts therefrom (subject as aforesaid) and may, at their expense, discuss the Lessee's affairs, finances and accounts with its executive officers, all at such times and as often as may be reasonably requested. None of the Lessor, the Equity Participant, the Indenture Trustee or any Collateral Trust Trustee shall have any duty whatsoever to make any inspection or inquiry

referred to in this Section 8(b) and shall not incur any liability or obligation by reason of not making any such inspection or inquiry.

(c) Capital Improvements. To the extent that Applicable Law or Prudent Utility Practice in respect of considerations of public health or safety requires that a Capital Improvement be made to Unit 2, the Lessee shall cause such Capital Improvement to be made in accordance with the ANPP Participation Agreement. If and to the extent required by the ANPP Participation Agreement, the Lessee shall, at its sole expense, promptly participate in the making of any Capital Improvement to Unit 2. Without the written consent of the Lessor, the Lessee shall not permit any Capital Improvement to be made during the last three years of the Lease Term unless the Lessee has exercised its option to purchase or renew as provided herein or unless (i) such Capital Improvement is reasonably expected to be completed prior to the end of the Lease Term, as determined by an independent engineer selected by the Lessee and reasonably acceptable to the Lessor, (ii) arrangements for the payment thereof satisfactory to the Equity Participant have been made and (iii) the Lessee is committed to pay the cost thereof (whether or not completed prior to the end of the Lease Term) in a manner satisfactory to the Equity Participant. The net proceeds of (i) any sale or other disposition of property removed from Unit 2 received (considering as part of such amount received any amount set off or deducted by any Person claiming a right against the Lessee to do so) by, or credited to the account of, the Lessee in accordance with the ANPP Participation Agreement and (ii) any insurance proceeds received (considering as part of such amount received any amount set off or deducted by any Person claiming a right against the Lessee to do so) for the account of the Lessor or the Lessee in respect of the loss or destruction of, or damage or casualty to, any such property, the Unit 2 Interest of such amount shall be applied as provided in Section 9(g), (h) or (i), as the case may be. The Unit 2 Interest in property at any time removed from Unit 2 shall remain the property of the Lessor, no matter where located, until such time as a Capital Improvement constituting a replacement of such property shall have been installed in Unit 2 or such removed property has been disposed of by the Operating Agent in accordance with the ANPP Participation Agreement. Simultaneously with such disposition by the Operating

Agent, title to the Unit 2 Interest in the removed property shall vest in the Person designated by the Operating Agent, free and clear of any and all claims or rights of the Lessor. Unless paragraph (3) of Section 8(e) shall be applicable, upon the incorporation of a Capital Improvement in Unit 2, without further act, (i) title to the Unit 2 Interest, in such Capital Improvement shall vest in the Lessor and (ii) such applicable undivided interest in such Capital Improvement shall become subject to this Facility Lease and be deemed to be part of the Undivided Interest for all purposes hereof to the same extent that the Lessor had a like undivided interest in the property originally incorporated or installed in Unit 2. The Lessee warrants and agrees that the Lessor's interest in all Capital Improvements shall be free and clear of all Liens, except Permitted Liens other than the type specified in clauses (ii), (iii) and (xii) of the definition thereof.

(d) Reports. To the extent permissible, the Lessee shall prepare and file in a timely fashion, or, where the Lessor shall be required to file, the Lessee shall prepare and deliver to the Lessor within a reasonable time prior to the date for filing, any reports with respect to Unit 2, the Undivided Interest or the condition or operation thereof that shall be required to be filed with any Governmental Authority. On or before March 1 of each year (commencing March 1, 1987) and on the Lease Termination Date, the Lessee shall furnish the Lessor and the Equity Participant with a report stating the total cost of all Capital Improvements and describing separately and in reasonable detail each Capital Improvement (or related group of Capital Improvements) made during the period from the date hereof to December 31, 1986, in the case of the first such report, and during the period from the end of the period covered by the last previous report to the December 31 prior to such report, in the case of subsequent reports. On or before March 1 in each year (commencing March 1, 1987) and at such other times as the Lessor or the Equity Participant shall reasonably request in writing, the Lessee will report in writing to the Lessor with respect to (i) the most recent annual capital expenditure budget submitted by the Operating Agent to the Lessee in accordance with the ANPP Participation Agreement and (ii) the current plans (if any) which the Lessee may have for the financing of the same under Section 8(f).

(e) Title to Capital Improvements. Title to the Unit 2 Interest in each Capital Improvement to Unit 2 shall vest as follows:

(1) in the case of each Nonseverable Capital Improvement, whether or not the Lessor shall have financed or provided financing (in whole or in part) for such Unit 2 Interest in such Capital Improvement by an Additional Equity Investment or a Supplemental Financing, or both, effective on the date such Capital Improvement shall have been incorporated or installed in Unit 2, the Lessor shall, without further act, acquire title to such Unit 2 Interest in such Capital Improvement;

(2) in the case of each Severable Capital Improvement, if the Lessor shall have financed (by an Additional Equity Investment or a Supplemental Financing, or both) the Unit 2 Interest of the cost of such Capital Improvement, the Lessor shall, without further act, acquire title to such undivided interest in such Capital Improvement; and

(3) in the case of each Severable Capital Improvement, if the Lessor shall not have financed (by either an Additional Equity Investment or a Supplemental Financing, or both) the Unit 2 Interest of the cost of such Capital Improvement, the Lessee shall retain title to such an undivided interest in such Capital Improvement.

Immediately upon title to such Unit 2 Interest in any Capital Improvement vesting in the Lessor pursuant to paragraph (1) or paragraph (2) of this Section 8(e), such Unit 2 Interest in such Capital Improvement shall, without further act, become subject to this Facility Lease and be deemed part of the Undivided Interest and Unit 2 for all purposes hereof.

(f) Funding of the Cost of Capital Improvements. Before placing in service any Capital Improvement to Unit 2 the cost of which exceeds \$100,000,000 in respect of the interests of all ANPP Participants, the Lessee shall give the Lessor and the Equity Participant reasonable advance notice thereof. The Equity Participant shall have the option, in its

sole discretion, of financing through the Lessor the Unit 2 Interest of the cost of any such Capital Improvement, or any other Capital Improvement presented to the Equity Participant for financing, including or not including the making of an investment by the Equity Participant (an Additional Equity Investment) and the issuance of Additional Notes, all on terms acceptable to the Lessee and the Equity Participant. If the Equity Participant does not finance, or arrange the financing of, the Unit 2 Interest of the cost of such Capital Improvement, the Lessee may cause the Lessor to issue, if and to the extent permitted by the Indenture, to one or more Persons (other than the Lessee or any Person affiliated with the Lessee within the meaning of section 318 of the Code) Additional Notes and to use the proceeds thereof to pay the applicable percentage of the cost of such Capital Improvement, subject, however, to the satisfaction of the following conditions:

(i) there shall be no more than one Supplemental Financing in any calendar year;

(ii) the sum of the Supplemental Financing Amounts in any calendar year shall equal or exceed the Unit 2 Interest of \$5,000,000;

(iii) the Lessee may include in any request for a Supplemental Financing only Capital Improvements not previously financed in any Supplemental Financing and which have been installed or affixed no earlier than three calendar years before the beginning of the calendar year in which such Supplemental Financing occurs;

(iv) the total amount of all Supplemental Financings during the Basic Lease Term shall not exceed the Lessor's Portion of \$200,000,000;

(v) unless waived by the Equity Participant, the Lessee shall, at the time of such Supplemental Financing, have outstanding at least one issue of its debt securities (which may include the Bonds) rated at least "investment grade", as determined by Standard & Poor's and Moody's, if the Lessee has debt securities rated by such rating organizations, or as determined by one of such rating

organizations, if the Lessee has debt securities rated by only one such organization, or, if neither of such rating organizations shall rate debt securities of the Lessee at the time, by any nationally recognized rating organization in the United States of America;

(vi) the sum of the Supplemental Financing Amount and any Additional Equity Investment shall not exceed that portion of the cost of Capital Improvements which, when financed, will constitute an addition to the Equity Participant's basis under Section 1012 or 1016 of the Code;

(vii) in the opinion of independent tax counsel to the Equity Participant, such Supplemental Financing shall not result in any adverse tax effect upon the Equity Participant or affect the status of the Facility Lease as a "true lease" for Federal income tax purposes, and the Equity Participant and the Lessee shall have agreed upon the amount and manner of payment of any indemnity payable by the Lessee as a consequence of such Supplemental Financing;

(viii) the Additional Notes shall have a final maturity date no later than December 30, 2015;

(ix) the Lessee shall have made such representations and warranties and covenants regarding the tax characteristics of the Lessor's undivided interest in each Capital Improvement as shall be mutually acceptable to the Lessee and the Equity Participant;

(x) appropriate adjustments to Basic Rent and the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values, and Modified Special Casualty Values shall have been agreed to by the Equity Participant to support the amortization of the Additional Notes issued in respect of such Supplemental Financing and to preserve Net Economic Return (without regard to any tax

benefits associated with such Capital Improvement);

(xi) the Lessee shall have paid to the Lessor an amount that on an After-Tax Basis will be equal to all out-of-pocket costs and expenses reasonably incurred by the Lessor or the Equity Participant and not financed as a part of such Supplemental Financing or reflected in adjustments to Basic Rent;

(xii) no Default or Event of Default shall have occurred and be continuing and no Event of Loss or Deemed Loss Event shall have occurred;

(xiii) the Lessee shall have entered into such agreements and shall have provided such tax indemnities, opinions, certificates and other documents as the Equity Participant shall reasonably request;

(xiv) unless and until the Indenture has been discharged, Additional Notes shall be issued under, and in compliance with the terms of, the Indenture; and

(xv) in the opinion of the Equity Participant, such Supplemental Financing shall not result in any material adverse effect on the Equity Participant's financial accounting position.

SECTION 9. Event of Loss; Deemed Loss Event.

(a) Damage or Loss. In the event that Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) shall become applicable, or an Event of Loss, a Requisition of Use or a Requisition of Title shall occur, or Unit 2 or any substantial part thereof shall suffer destruction, damage, loss, condemnation, confiscation, theft or seizure for any reason whatsoever, such fact shall promptly, and in any case within five Business Days following any such event, be reported by the Lessee to the Lessor and the Equity Participant.

(b) Repair. The Lessee shall promptly make any and all payments required of the Lessee under the

provisions of the ANPP Participation Agreement relating to damage or destruction or the like to Unit 2 or any portion thereof; provided, however, that the Lessee shall in no event be obligated to make or join in any agreement under Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) concerning repairs to or reconstruction of Unit 2.

(c) Payment of Casualty Value. On the date next following the occurrence of an Event of Loss specified in a notice from the Lessor to the Lessee, the Lessee shall pay to the Lessor all Basic Rent due on, or accrued Basic Rent to, such date, plus an amount equal to the excess of (x) Casualty Value, determined as of the date such payment is due, if such date is a Basic Rent Payment Date, or the immediately preceding Basic Rent Payment Date, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from such Basic Rent Payment Date to such date of payment, over (y) the unpaid principal amount of the Notes Outstanding on such date and assumed by the Lessee on such date, after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of such Notes on such date. If the Lessee shall have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued the Bank Exchange Notes as provided in such Section), the Lessor shall, as long as no Default or Event of Default shall have occurred and be continuing (and at any time after the occurrence of an Event of Loss the Lessor may):

(i) if Section 16.2 of the ANPP Participation Agreement (as in effect on the date hereof) shall be applicable and the Lessee shall have declined, but one or more of the other ANPP Participants shall have elected, to reconstruct or restore Unit 2, as permitted by the ANPP Participation Agreement, Transfer the Undivided Interest and the Real Property Interest to such electing ANPP Participants, as required by, and in the proportions set forth in, the ANPP Participation Agreement, in which case any amounts received by the Lessee in respect of the Lessor's Portion of the "salvage value" purchase price payable by such ANPP Participant to the Lessee in respect of Unit 2 (considering as part of

such amount received any amount set off or deducted by such Person as a result of a claim or right against the Lessee shall be applied (A) to reduce the Lessee's obligation to pay the amounts required to be paid by the Lessee pursuant to this paragraph or, if already paid, to reimburse the Lessee for such payment, and (B) the balance if any, of such payments shall be divided between the Lessee and the Lessor as their interests may appear); or

(ii) in all other cases Transfer the Undivided Interest and the Real Property Interest to the Lessee.

If the Lessee shall have made such payment but shall not have assumed the obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued the Bank Exchange Notes as provided in such Section), the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount, payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding, and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law.

(d) Payment of Special Casualty Value. If events giving rise to a Deemed Loss Event shall occur, the party hereto having knowledge thereof shall promptly notify the other party of the occurrence thereof. At any time thereafter, the Lessor may demand, by written notice to the Lessee, that the Lessee pay, and the Lessee shall pay, on the date specified in such notice, to the Lessor all Basic Rent due on, or accrued Basic Rent to, such date, plus an amount equal to the excess of (x) Special Casualty Value, determined as of the date such payment is due, if such date is a Basic Rent Payment Date, or the immediately preceding Basic Rent Payment Date, in all other cases, plus, in the latter case, interest thereon at the Prime Rate from such Basic Rent Payment Date to such date of payment, over (y) the unpaid principal amount of the Notes Outstanding on such date, after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of the Notes on such date. If the Lessee shall

have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or shall have issued Bank Exchange Notes as provided therein), the Lessor shall, so long as no Default or Event of Default shall have occurred and be continuing (and at any time after the occurrence of a Deemed Loss Event the Lessor may), Transfer the Undivided Interest and the Real Property Interest to the Lessee. If the Lessee shall have made such payment but shall not have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture (or issued Bank Exchange Notes as provided therein), the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount, payable on each Basic Rent Payment Date thereafter, equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes Outstanding, and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law.

(e) Requisition of Use. In the case of a Requisition of Use not constituting an Event of Loss, this Facility Lease shall continue, and each and every obligation of the Lessee hereunder and under each Transaction Document shall remain, in full force and effect. So long as no Default or Event of Default shall have occurred and be continuing, the Lessee shall be entitled to all sums received by reason of any such Requisition of Use for the period ending on the Lease Termination Date, and the Lessor shall be entitled to all sums received by reason of any such Requisition of Use for the period after the Lease Termination Date.

(f) Termination of Lease Term. Upon (but only upon) a Transfer by the Lessor pursuant to Section 9(c) or 9(d) to the Lessee, the Lessee's assumption of all remaining obligations and liabilities of the Owner Trustee under the Indenture and the Notes and payment of the amounts specified therein, the Lease Term shall end and the Lessee's obligation to pay Basic Rent after such Transfer shall cease, but the Lessee shall continue to be required to make all payments of Supplemental Rent as and when due. In all other cases, the Lease Term shall continue and this Facility Lease shall remain in full force and effect.

(g) Application of Payments on an Event of Loss. Any payments received at any time by the Lessor or the Lessee (other than insurance placed by the Owner Trustee or the Equity Participant pursuant to Section 10(b)) from any Governmental Authority, insurer or other Person (except the Lessee) as a result of the occurrence of an Event of Loss (considering as part of such amount received any amount which was set off or deducted therefrom as a result of a claim by any Person against the Lessee) shall be applied as follows:

(i) all such payments shall be promptly paid to the Lessor for application pursuant to the following provisions of this Section 9(g), except that the Lessee may retain any amounts that would at the time be payable to the Lessee as reimbursement under the provisions of clause (ii) below;

(ii) so much of such payments as shall not exceed the amount required to be paid by the Lessee pursuant to Section 9(c) (ignoring, for this purpose, clause (ii) of the first sentence thereof) shall be applied in reduction of the Lessee's obligation to pay such amount if not already paid by the Lessee or, if already paid by the Lessee, shall be applied to reimburse the Lessee for its payment of such amount; and

(iii) the balance, if any, of such payments, in the case of payments from insurance carried by or on behalf of the Lessee shall be paid to the Lessee or, in the case of any other payments, shall be divided between the Lessor and the Lessee as their interests may appear.

(h) Application of Payments Not Relating to an Event of Loss. Payments received (considering as part of such amount received any amount which was set off or deducted therefrom as a result of a claim by any Person against the Lessee) at any time by the Lessor, the Lessee or the Equity Participant (other than insurance placed by the Owner Trustee or the Equity Participant pursuant to Section 10(b)) from any insurer or other Person with respect to any event giving rise to an amount referred to in the second sentence of Section 6(c) or the third sentence of Section 8(c), destruction, damage, loss, condemnation, confiscation,

theft or seizure of or requisition of title to Unit 2, the Undivided Interest or the Real Property Interest or any part thereof, in each case not constituting an Event of Loss shall be applied first to reimburse the Lessee for all amounts expended by it pursuant to Section 9(b) and second, the balance, if any, of such payments shall, in the case of payments from insurance carried by or on behalf of the Lessee, be paid to the Lessee or, in the case of other payments, be divided between the Lessor and the Lessee as their interests may appear.

(i) Dispositions at Time of Default or Event of Default. Notwithstanding the foregoing provisions of this Section 9, if a Default or an Event of Default shall have occurred and be continuing, any amount that would otherwise be payable to or for the account of, or that would otherwise be retained by, the Lessee pursuant to Section 10 or this Section 9 shall be paid to the Lessor as security for the obligations of the Lessee under this Facility Lease and, at such time thereafter as the Lessee shall have cured any such Default or Event of Default, such amount shall be paid promptly to the Lessee unless this Facility Lease shall have theretofore been declared to be in default, in which event such amount shall be disposed of in accordance with the provisions hereof and of the Indenture.

SECTION 10. Insurance.

(a) Required Insurance. The Lessee will cause the Operating Agent to carry and maintain at least the following insurance coverage with respect to the Undivided Interest and the Real Property Interest, in each case with insurers of recognized responsibility, in such form as shall be satisfactory to the Equity Participant.

(1) Non-Nuclear Insurance. The Lessee shall maintain:

(i) "all risk" property insurance covering physical loss with respect to Unit 2 in such amounts and with such other terms as are required by or are in accordance with Prudent Utility Practice, but in no event shall such amounts be less than the estimated maximum probable loss in respect of such property. Any insurance carried in accordance with this

Section 10(a)(1)(i) shall be endorsed to provide that:

(A) losses shall be adjusted and paid as provided in Section 10(a)(4);

(B) the Lessor and the Equity Participant (the "Additional Insureds") (i) are included as additional insureds, as their interests may appear and (ii) any obligation imposed upon the insured (including without limitation the liability to pay premiums) shall be the sole obligation of the Lessee and not that of any Additional Insured;

(C) the respective interests of the Additional Insureds shall not be invalidated by any breach of any warranties by the ANPP Participants contained in such policies;

(D) the insurer thereunder waives all rights of subrogation against the Additional Insureds with respect to their respective interests in Unit 2;

(E) such insurance shall be primary without right of contribution of any other insurance carried by or on behalf of any Additional Insured with respect to its interest in Unit 2; and

(F) if such insurance is cancelled for any reason whatsoever including non-payment of premium or any substantial change is made in the coverage which affects the interest of the Additional Insureds, (1) such cancellation or change shall not be effective as to the Additional Insureds for 30 days after receipt by The First National Bank of Boston, as Owner Trustee and agent, of written notice from such insurer of such cancellation or change, and (2) the Lessee will use its best efforts to cause such insurer to deliver a certificate with respect to such cancellation or

change to the Equity Participant and the Indenture Trustee.

(ii) bodily injury and property damage liability insurance (including product liability, completed operations and personal injury insurance) covering claims arising out of the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site. The amount and other terms of such insurance shall be in accordance with the higher of Prudent Utility Practice and the ANPP Participation Agreement, but such limits shall in no event be less than \$25,000,000 per occurrence combined bodily injury and property damage. Such insurance may include deductible amounts not to exceed \$5,000,000. Any insurance carried in accordance with this Section 10(a)(1)(ii) shall be endorsed as provided in paragraphs (B), (C), (D), (E) and (F) of Section 10(a)(1)(i), except that the term "Additional Insureds" wherever it appears shall include the Lessor, the Equity Participant and all Indemnitees.

(2) Nuclear Insurance. The Lessee shall maintain:

(i) nuclear property insurance in amounts and with such other terms as are required by or are in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement and (c) Prudent Utility Practice; provided, however, that such insurance shall at all times be maintained in amounts at least equal to the maximum nuclear property insurance available on commercially reasonable terms. The coverage afforded by such nuclear property insurance in respect of any loss at PVNGS and available for any loss at Unit 2, either (A) shall at all times be at least equal to \$750 million regardless of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of Nuclear Incident) or (B) so long as (1) Unit 2 is in, or is in a procedure which will result in, a state of cold shutdown in accordance with Prudent Utility Practice and (2) the first mortgage

bonds of the Lessee shall have an investment grade rating (x) by two nationally accepted rating agencies if such first mortgage bonds are rated by two nationally accepted rating agencies or (y) by one nationally accepted rating agency if such first mortgage bonds are only rated by one nationally accepted rating agency, will be reinstated to be equal to at least \$750 million within 180 days of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of a Nuclear Incident). Such insurance may include deductible amounts not to exceed \$10,000,000. Any insurance carried in accordance with this Section 10(a)(2)(i) shall be endorsed by the insurer as provided in paragraphs (A), (B), (D), (E) and (F) of Section 10(a)(1)(i).

(ii) the maximum nuclear liability insurance in amounts and such other terms as required by or in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement, (c) Prudent Utility Practice and (d) the maximum nuclear liability insurance available on commercially reasonable terms, but in any event in such amounts and containing such other terms as to cover the "aggregate liability" for a single "nuclear incident" of all "persons indemnified" (as such terms are used in the Atomic Energy Act) and in connection with the ownership, maintenance, condition or use of Unit 2 and the PVNGS Site. The Lessee shall also maintain supplier's and transporter's insurance in amounts consistent with Prudent Utility Practice. The Lessee shall maintain nuclear liability insurance pursuant to this Section 10(a)(2)(ii), whether or not the Lease Termination Date shall have occurred, until notified by the Equity Participant that neither the Lessor nor the Equity Participant has any further real or potential liability in connection with the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site; provided that after Decommissioning has been completed the Lessee shall not be required to maintain nuclear liability insurance for more than 30 years.

Any insurance carried in accordance with this Section 10(a)(2)(ii) shall be endorsed as provided in paragraphs (B); (D), (E) and (F) of Section 10(a)(1)(i).

(iii) the Lessee shall, or shall cause the Operating Agent to, use its best efforts at all times to obtain the endorsement referred to in paragraph (C) of Section 10(a)(1)(i) on all insurance referred to in this Section 10(a)(2), and shall cause such endorsement to be obtained if and to the extent it is available to any other owner or operator of a nuclear generating unit.

(3) Annual Reports and Certificates. The Lessee shall, on or before March 1 of each year, commencing March 1, 1987, furnish to the Lessor and the Equity Participant (A) a report signed by the broker or brokers for the PVNGS insurance (or if insurance is placed directly by the Operating Agent, a report signed by the Operating Agent which will include a copy of the certificate of insurance signed by the carrier, which certificate shall indicate that all endorsements required by this Section 10 are applicable) (i) describing in detail the insurance then maintained by the ANPP Participants with respect to PVNGS, (ii) stating that no premiums are then delinquent, and (iii) stating that insurance maintained is in accordance with (1) the ANPP Participation Agreement and (2) this Section 10; (B) a report signed by the broker or brokers for the Lessee's insurance (or if insurance is placed directly by the Lessee, a report signed by the Lessee which will include a copy of the certificate of insurance signed by the carrier, which certificate shall indicate that all endorsements required by this Section 10 are applicable) showing the separate insurance, if any, then maintained by the Lessee with respect to its interest in PVNGS and stating that no premiums under such insurance are delinquent; (C) a certificate signed by the Lessee stating that the insurance maintained by the ANPP Participants and by the Lessee, identified on the reports to be delivered pursuant to clauses (A) and (B), is in accordance with Prudent Utility Practice within the nuclear industry, the ANPP Participation Agreement and this Section 10; and (D) upon the request of the Lessor or the Equity

Participant, copies (to the extent permitted by the issuers of such policies) of policies so maintained. Any report by an insurance broker with respect to clause (A)(iii)(1) may be made in reliance upon a schedule provided by the Lessee (a copy of which shall be attached) identifying the insurance (by coverage, limits, insureds and other pertinent details) required to be maintained under the ANPP Participation Agreement. Any report with respect to clause (A)(iii)(2) may be made in reliance upon a similar schedule provided by the Lessee (a copy of which shall be attached) identifying the insurance required to be maintained under this Section 10.

(4) Proceeds. All insurance proceeds paid in respect of or pursuant to paragraphs (1) and (2) above shall (i) be applied as provided in Section 9(g), (h) or (i), as the case may be, and (ii) be adjusted with the insurance companies or otherwise collected, including the filing of appropriate proceedings, by the Operating Agent in accordance with the ANPP Participation Agreement subject, however, to any priority allocations of such proceeds to decontamination and debris removal set forth in the insurance policies or required under Applicable Law. If the Operating Agent, as trustee, shall become the loss payee under any policy of insurance constituting "Project Insurance", as such term is defined in the ANPP Participation Agreement, then the Lessor and the Equity Participant shall be made beneficiaries of the trust arrangement under which the Operating Agent acts as trustee.

(b) Permitted Insurance. Nothing in this Section 10 shall prohibit the Lessee from placing at its expense insurance on or with respect to the cost of purchasing replacement power, naming the Lessee as insured and/or loss payee, unless such insurance would conflict with or otherwise limit the availability of insurance to be provided or maintained in accordance with Section 10(a). Nothing in this Section 10 shall prohibit the Lessor or the Equity Participant from placing at its expense other insurance on or with respect to Unit 2, the Undivided Interest or the Real Property Interest or the operation of Unit 2, naming the Lessor or the Equity Participant as insured and/or loss payee, unless such insurance would conflict with or otherwise limit the

insurance to be provided or maintained in accordance with Section 10(a).

SECTION 11. Rights to Assign or Sublease.

(a) Assignment or Sublease by the Lessee. Without the prior written consent of the Lessor, the Lessee shall not encumber (except for Permitted Liens), or assign, sublease or transfer (except to a Surviving Lessee in a transaction which meets the requirements of Section 10(b)(3)(ii) of the Participation Agreement), its leasehold interest under this Facility Lease in the Undivided Interest or the Real Property Interest, except that the Lessee may assign its leasehold interest under this Facility Lease in the Undivided Interest and the Real Property Interest to a wholly owned subsidiary of the Lessee or of the Lessee's parent if such subsidiary's obligations under this Facility Lease and the other Transaction Documents and the Financing Documents, if then in effect, shall be guaranteed by APS pursuant to a valid and enforceable guarantee containing appropriate covenants of APS and otherwise satisfactory in form and substance to the Equity Participant in its absolute discretion. The Lessee shall not, without the prior written consent of the Lessor and the Equity Participant, part with the possession of, or suffer or allow to pass out of its possession, the Undivided Interest or the Real Property Interest or any interest therein, except to the extent required pursuant to the ANPP Participation Agreement or as expressly permitted by the provisions of this Facility Lease (including, without limitation, the first sentence of this Section 11(a)).

(b) Assignment by Lessor as Security for Lessor's Obligations. To secure the indebtedness evidenced by the Notes, the Lessor will assign to the Indenture Trustee (x) its right, title and interest in and to this Facility Lease, including the right to receive all payments of Rent (other than Excepted Payments and Excepted Rights), to the extent provided in the Indenture and (y) its right, title and interest in and to the Undivided Interest and the Real Property Interest. The Lessee hereby (a) consents to such assignment and to the terms of the Indenture, (b) agrees to pay directly to the Indenture Trustee at the Indenture Trustee's Office (so long as the lien of the Indenture has not been satisfied and discharged and the Lessor is obligated thereunder) all amounts of Rent

(other than Excepted Payments) due or to become due to the Lessor that shall be required to be paid to the Indenture Trustee pursuant to the Indenture, (c) agrees that the right of the Indenture Trustee to any such payments shall be absolute and unconditional and shall not be affected by any circumstances whatsoever, including, without limitation, those circumstances set forth in Section 4, and (d) agrees that, to the extent provided in the Indenture and until the Indenture is discharged in accordance with its terms, the Indenture Trustee shall have all the rights of the Lessor hereunder (other than Excepted Rights and the right to receive Excepted Payments) as if the Indenture Trustee had originally been named herein as the Lessor. Following any Transfer by Lessor or purchase by Lessee of the Undivided Interest and the Real Property Interest, the Undivided Interest and the Real Property Interest shall (unless the Notes shall have been paid in full) remain subject to the lien of the Indenture and such lien shall continue as an existing, valid and enforceable first lien on the Undivided Interest and the Real Property Interest.

SECTION 12. Lease Renewal.

(a) Fixed Rate Renewal Term. Subject to the notice requirements set forth in Section 13(a), at the end of the Basic Lease Term, provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee shall have the right to renew the term of this Facility Lease (i) for a period commencing January 1, 2016, and ending midnight on December 31, 2017 (such period and any extension thereof pursuant to clause (ii) of this paragraph (a) being herein referred to as the Fixed Rate Renewal Term); and (ii) if it has elected the Fixed Rate Renewal Term, for an extension period commencing on January 1, 2018 and which expires not later than the last day of the Maximum Option Period.

(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided, that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of

Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period not to exceed 2 years (herein referred to as the Fair Market Renewal Term; and the Fixed Rate Renewal Term (including any extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in which case Basic Rent payable during such Fair Market Renewal Term shall be the Fair Market Rental Value of the Undivided Interest.

SECTION 13. Notices for Renewal or Purchase; Purchase Options.

(a) Expiration of Basic Lease Term. Not earlier than five nor later than three years prior to the expiration date of the Basic Lease Term the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(a) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration date of the Basic Lease Term as the case may be, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(b) or (y) the option to renew this Facility Lease for the Fixed Rate Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor if, on the date a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(a), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such Fair Market Sales Value shall be determined by the Appraisal Procedure. In the case of the exercise of the option for the Fixed Rate Renewal Term, the Maximum Option Period shall be determined by the Appraisal Procedure.

(b) Expiration of Fixed Rate Renewal Term. Not earlier than five years and later than three years prior

to the expiration date of the Fixed Rate Renewal Term, if elected, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(b) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration of the Fixed Rate Renewal Term the Lessee will give the Lessor written notice of its election to exercise (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fair Market Renewal Term. Any such election shall be irrevocable as to the Lessee (except as hereinafter provided), but no such election shall be binding on the Lessor, if, on the effective date thereof, an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(b), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value and the Fair Market Rental Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such values shall be determined by the Appraisal Procedure.

(c) Purchase Option at Expiration of the Lease Term. Subject to the notice requirements set forth in Section 13(a) or 13(b), as the case may be, provided that no Event of Default shall have occurred and be continuing, no Event of Loss or Deemed Loss Event shall have occurred and the Notes shall have been paid in full, the Lessee shall have the right to purchase the Undivided Interest on the date of the expiration of the Basic Lease Term or the then applicable Renewal Term (if elected), for a purchase price equal to the Fair Market Sales Value thereof.

(d) Purchase of the Undivided Interest; Payment, Etc. If the Lessee shall have elected to purchase the Undivided Interest pursuant to Section 13(c), payment by the Lessee of the purchase price therefor shall be made in immediately available funds, whereupon

the Lessor shall Transfer the Undivided Interest and the Real Property Interest to the Lessee.

(e) Acquisition of Additional Capacity. The Lessee agrees not to acquire or lease any additional capacity from PVNGS during the five years preceding the expiration of the Basic Lease Term unless at the time of such acquisition or lease, the Lessee has exercised its option to renew this Facility Lease or purchase the Undivided Interest.

SECTION 14. Termination for Obsolescence.

(a) Termination Notice. Unless a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred, if the Board of Directors of the Lessee shall have adopted a resolution to the effect that Unit 2 is surplus to the Lessee or economically obsolete and provided that the Lessee is making a good faith effort to sell any ownership interest which it may have in Unit 2, the Lessee shall deliver a written notice (a Termination Notice) to the Lessor, the Equity Participant and the Indenture Trustee (which notice shall be irrevocable), to terminate this Facility Lease on any Basic Rent Payment Date after December 30, 1996, and prior to December 30, 2012 (the Termination Date), which date shall not be earlier than one year from the date of such notice. If the Lessee shall give the Lessor a Termination Notice, the Lessee shall, as agent for the Lessor, use its best efforts to obtain cash bids for the purchase of the Undivided Interest and the Real Property Interest, together with the interest of the Lessor under the Assignment and Assumption. The Lessor shall also have the right to obtain such cash bids, either directly or through agents other than the Lessee. The Lessee shall certify to the Lessor within ten days after the Lessee's receipt of each bid (and, in any event, prior to the Termination Date) the amount and terms thereof and the name and address of the Person (which shall not be the Lessee or any Affiliate of the Lessee or any agent of any thereof) submitting such bid.

(b) Right of Lessor to Retain Undivided Interest upon Termination. The Lessor may elect to retain, rather than sell, the Undivided Interest and the Real Property Interest by giving notice to the Lessee and the Indenture Trustee prior to the Termination Date. It shall be a condition precedent to the Lessor's

right to retain the Undivided Interest and the Real Property Interest that on or prior to the Termination Date the Lessor shall have paid (or made provision for payment) to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on such date and all premium, if any, and interest accrued and unpaid on the date of payment. If the Lessor elects to retain the Undivided Interest and the Real Property Interest pursuant to this Section 14(b), the Lessee shall pay to the Lessor on the Termination Date the Basic Rent and any other Rent due or accrued, as the case may be, to and including the Termination Date, together with an amount equal to the excess, if any, of the Special Casualty Value as of the Termination Date over the highest bona fide offer received pursuant to Section 14(a).

(c) Events on the Termination Date. If the Lessor has not elected to retain the Undivided Interest as provided in Section 14(b), on the Termination Date the Lessor shall (but only upon receipt of the sale price and all additional payments specified in the next sentence) Transfer the Undivided Interest for cash to the bidder (which shall not be the Lessee or an Affiliate of the Lessee or any agent of any thereof) that shall have submitted the highest bid on or before the Termination Date. The total sale price realized at such sale shall be retained by the Lessor (subject, however, to the terms of the Indenture and the requirement that there shall have been paid, or provision for payment made, to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on the Termination Date and all premium, if any, and interest accrued and unpaid on the date of payment) and, in addition, on the Termination Date the Lessee shall pay to the Lessor (A) the excess, if any, of the Special Casualty Value as of the Termination Date over the net sale price of the Undivided Interest and (B) any Basic Rent due or accrued, as the case may be, to and including the Termination Date, and shall pay to the Person or Persons entitled thereto all Supplemental Rent (other than Special Casualty Value). Upon compliance by the Lessee with the applicable provisions of this Section 14, the obligation of the Lessee to pay Basic Rent for any period after the Termination Date shall cease and the Basic Lease Term shall end on the Termination Date but the obligations of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination. If, other than as a result of the Lessor's

election to retain the Undivided Interest and the Real Property Interest as provided in Section 14(b), on or as of the Termination Date no such sale shall occur or the Lessee shall not have complied in full with this Section 14, this Facility Lease shall continue in full force and effect in accordance with its terms except that the Lessee shall be entitled to deliver one other Termination Notice provided that such second Termination Notice shall not occur during the 3-year period following such Termination Date. The Lessor shall be under no duty to solicit bids, to inquire into the efforts of the Lessee to obtain bids or otherwise take any action in connection with any such sale, other than, if the Lessor has not elected to retain the Undivided Interest, to Transfer the Undivided Interest and the Real Property Interest to the purchaser named in the highest bid certified by the Lessee to the Lessor or obtained by the Lessor, against receipt of the payments provided for herein.

(d) Early Termination. If the Lessee shall fail to exercise its renewal option or purchase option within the time provided by Section 13(a) or 13(b), the Lessor shall have the option, on any Basic Rent Payment Date thereafter, on at least one year's prior written notice (an Early Termination Notice) to the Lessee and the Indenture Trustee, to terminate this Facility Lease on the Basic Rent Payment Date specified in such notice (the Early Termination Date). Any Early Termination Notice may be revoked by the Lessor at any time on or prior to the 30th day preceding the Early Termination Date (the Early Termination Commitment Date), after which the Lessor shall be irrevocably committed to terminate this Facility Lease on the Early Termination Date. On or prior to the Early Termination Commitment Date, the Lessor shall deposit with the Indenture Trustee cash in an amount (or a letter of credit of an Eligible Bank for such amount) equal to the unpaid principal amount of all Notes outstanding on such date and all premium, if any, and interest accrued and to accrue on and as of the Early Termination Date. On the Early Termination Date, the Lessee shall pay to the Lessor any Basic Rent due or accrued, as the case may be, to and including the Early Termination Date, and shall pay to the Person or Persons entitled thereto all Supplemental Rent (excluding from such Supplemental Rent any amount due and owing with respect to principal of, and premium, if any, on the Notes being prepaid on such date, other than any amount of principal which would have been paid

on such date if such Notes were not being prepaid), whereupon the obligation of the Lessee to pay any Basic Rent for any period after the Early Termination Date shall cease and the Lease Term shall end, but the obligations of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination.

SECTION 15. Events of Default.

The term Event of Default, wherever used herein, shall mean any of the following events (whatever the reason for such Event of Default and whether it shall be voluntary or involuntary, or come about or be effected by operation of law, or be pursuant to or in compliance with any Applicable Law or Governmental Action):

(i) the Lessee shall fail to make, or cause to be made, (x) payment of Casualty Value, Extraordinary Casualty Value or Special Casualty Value when due or payment due pursuant to exercise of the Cure Option when due, (y) any payment of Basic Rent within 5 days after the same shall become due or (z) any payment of Supplemental Rent (other than Casualty Value, Extraordinary Casualty Value or Special Casualty Value, or payment due pursuant to exercise of the Cure Option) within 20 days after the same shall become due or demanded, as the case may be; or

(ii) the Lessee shall fail to perform or observe any covenant, condition or agreement to be performed or observed by it under Section 10(b)(3)(i) or 10(b)(3)(ii) of the Participation Agreement or Section 7 or 11 of this Facility Lease; or

(iii) the Lessee shall fail to perform its agreements set forth in Section 5; or

(iv) the Lessee shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 10(b)(3)(v) of the Participation Agreement and such failure shall continue for a period of 15 days after there shall have been given to the Lessee by the Lessor or the Equity Participant

a notice specifying such failure and requiring it to be remedied and stating that such notice is a Notice of Default hereunder; or

(v) the Lessee shall fail to perform or observe any covenant, condition or agreement (other than those referred to in clauses (i) through (iv) above) to be performed or observed by it under this Facility Lease (other than Section 10) or any other Transaction Document, and such failure shall continue for a period of 30 days after there shall have been given to the Lessee by the Lessor or the Equity Participant a notice specifying such failure and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder; or

(vi) any representation or warranty made by the Lessee in this Facility Lease, any other Transaction Document (other than the Tax Indemnification Agreement) or any agreement, document or certificate delivered by the Lessee in connection herewith or therewith (other than in Section 7(b)(4) of the Participation Agreement) shall prove to have been incorrect in any material respect when any such representation or warranty was made or given and shall remain material and materially incorrect at the time in question; or

(vii) the Lessee shall commence a voluntary case or other proceeding seeking liquidation, reorganization or other relief with respect to itself or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, or shall consent to any such relief or to the appointment of or taking of possession by any such official in an involuntary case or other proceeding commenced against it, or shall make a general assignment for the benefit of creditors, or shall take any corporate action to authorize any of the foregoing; or an involuntary case or other proceeding shall be commenced against the Lessee seeking liquidation, reorganization

or other relief with respect to it or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, and such involuntary case or other proceeding shall remain undismissed or unstayed for a period of 60 consecutive days; or

(viii) final judgment for the payment of money in excess of \$10,000,000 shall be rendered against the Lessee and the Lessee shall not have discharged the same or provided for its discharge in accordance with its terms or bonded the same or procured a stay of execution thereof within 60 days from the entry thereof; or

(ix) (1) a default by the Lessee under the ANPP Participation Agreement in consequence of which the Lessee's right to receive its Generation Entitlement Share is suspended by the other ANPP Participants or (2) the giving by any ANPP Participant of a notice under Section 23.2 (or any comparable successor provision) of the ANPP Participation Agreement respecting a default thereunder by the Lessee and the lapse of 15 Business Days from the giving of such notice without the Lessee having cured such default; provided, however, that for purposes of this clause (2) if the Lessee shall have disputed the existence or nature of a default and such dispute shall have become the subject of an arbitration under Section 24 (or any comparable successor provision) of the ANPP Participation Agreement, such 15 Business Day period shall commence on the date of the final determination of the board of arbitrators under such provision; or

(x) (1) the Lessee shall fail to pay when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) any Debt of the Lessee the principal amount (or equivalent) of which is greater than \$20,000,000), and such failure shall continue

after the applicable grace period, if any, specified in the agreement or instrument relating to such Debt; or (2) any other default under any agreement or instrument relating to any such Debt, or any other event, shall occur and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such default or event is to accelerate the maturity of such Debt; or

(xi) the Lessee (A) shall fail, at any time, to provide or maintain a Letter of Credit which complies with all of the terms and conditions of Section 10(b) (3)(ix) of the Participation Agreement or (B) shall fail to provide a renewal or replacement Letter of Credit so complying (1) not less than 30 days prior to the stated termination date of an existing Letter of Credit, (2) within 20 days after the receipt by the Lessor of notice that an existing Letter of Credit will be terminated prior to its stated termination date under circumstances in which at least 30 days' notice of such termination is required or (3) concurrently with the receipt by the Lessor of notice that an existing Letter of Credit will be terminated prior to its stated termination date under circumstances in which less than 30 days' notice of such termination is required.

SECTION 16. Remedies.

(a) Remedies. Upon the occurrence of any Event of Default and so long as the same shall be continuing, the Lessor may, to the extent permitted by Applicable Law, exercise one or more of the following remedies, except as hereinbelow expressly otherwise set forth, as the Lessor in its sole discretion shall elect:

(i) the Lessor may declare this Facility Lease to be in default by written notice to such effect given to the Lessee, or may, by notice to the Lessee, rescind or terminate this Facility Lease;

(ii) the Lessor may (x) demand that the Lessee, and thereupon the Lessee shall, return possession of the Undivided Interest and the

Real Property Interest promptly to the Lessor in the manner and condition required by, and otherwise in accordance with the provisions of, this Facility Lease as if the Undivided Interest and the Real Property Interest were being returned at the end of the Lease Term, and the Lessor shall not be liable for the reimbursement of the Lessee for any costs and expenses incurred by the Lessee in connection therewith or (y) enter upon the PVNGS Site and take immediate possession of (to the exclusion of the Lessee) the Undivided Interest and the Real Property Interest, by summary proceedings or otherwise, all without liability to the Lessee for or by reason of such entry or taking of possession, whether for the restoration of damage to property caused by such taking or otherwise;

(iii) the Lessor may sell the Undivided Interest and the Real Property Interest, or any part thereof, together with any interest of the Lessor under the Assignment and Assumption or in respect of the Real Property Interest, at public or private sale, as the Lessor may determine, free and clear of any rights of the Lessee and without any duty to account to the Lessee with respect to such action or inaction or any proceeds with respect thereto (except to the extent required by clause (v) or (vi) below if the Lessor shall elect to exercise its rights thereunder), in which event the Lessee's obligation to pay Basic Rent hereunder for periods commencing after the date of such sale shall be terminated or proportionately reduced, as the case may be (except to the extent that Basic Rent is to be included in computations under clause (v) or (vi) below if the Lessor shall elect to exercise its rights thereunder);

(iv) the Lessor may hold, keep idle or lease to others all or any part of the Undivided Interest and the Real Property Interest, as the Lessor in its sole discretion may determine, free and clear of any rights of the Lessee and without any duty to account to the Lessee with respect to such action or

inaction or for any proceeds with respect to such action or inaction, except that the Lessee's obligation to pay Basic Rent for periods commencing after the Lessee shall have been deprived of use of the Undivided Interest and the Real Property Interest pursuant to this clause (iv) shall be reduced by an amount equal to the net proceeds, if any, received by the Lessor from leasing the Undivided Interest and the Real Property Interest to any Person other than the Lessee for the same periods or any portion thereof;

(v) except in the case of an Event of Default specified in clause (iii) of Section 15 (subject, however, to the proviso to the first sentence of Section 16(c) hereof), the Lessor may, whether or not the Lessor shall have exercised or shall thereafter at any time exercise its rights under clause (i), (ii), (iii) or (iv) above, demand, by written notice to the Lessee specifying a payment date which shall be a Basic Rent Payment Date not earlier than 10 days after the date of such notice, that the Lessee pay to the Lessor, and the Lessee shall pay to the Lessor, on the Basic Rent Payment Date specified in such notice, as liquidated damages for loss of a bargain and not as a penalty (in lieu of the Basic Rent due after the Basic Rent Payment Date specified in such notice), any unpaid Rent due through the Basic Rent Payment Date specified in such notice plus whichever of the following amounts the Lessor, in its sole discretion, shall specify in such notice together with interest on such amount at the interest rate specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice to the date of actual payment):

(A) an amount equal to the excess, if any, of (1) Casualty Value, computed as of the Basic Rent Payment Date specified in such notice, over (2) the Fair Market Rental Value of the Undivided Interest (determined on the basis of the then actual condition of Unit 2) until the end of the remaining useful life of

Unit 2, after discounting such Fair Market Rental Value semi-annually to present value as of the Basic Rent Payment Date specified in such notice at a rate of 10% per annum;

(B) an amount equal to the excess, if any, of (1) such Casualty Value over (2) the Fair Market Sales Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) as of the Basic Rent Payment Date specified in such notice; or

(C) an amount equal to the excess, if any, of (1) the present value as of the Basic Rent Payment Date specified in such notice of all installments of Basic Rent until the end of the Basic Lease Term or the Renewal Term, as the case may be, discounted semiannually at a rate of 10% per annum, over (2) the present value as of such Basic Rent Payment Date of the Fair Market Rental Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) until the end of the Basic Lease Term or the Renewal Term, as the case may be, discounted semiannually at a rate of 10% per annum;

(D) an amount equal to the highest of (1) such Casualty Value, (2) such discounted Fair Market Rental Value and (3) such Fair Market Sales Value and, in this event, upon full payment by the Lessee of all sums due hereunder, the Lessor shall, at its option, either Transfer the Undivided Interest and the Real Property Interest to the Lessee, or promptly sell the Undivided Interest and the Real Property Interest and pay over to the Lessee the net proceeds thereof up to the amount set forth in (1), (2) or (3) above actually paid by the Lessee to the Lessor;

(vi) if the Lessor shall have sold all the Undivided Interest and the Real Property Interest pursuant to clause (iii) above, the Lessor, in lieu of exercising its rights under clause (v) above, may, if it shall so elect, except in the case of an Event of Default specified in clause (iii) of Section 15, demand that the Lessee pay to the Lessor and the Lessee shall pay to the Lessor on the date of such sale, as liquidated damages for loss of a bargain and not as a penalty (in lieu of Basic Rent due for periods commencing after the next Basic Rent Payment Date following the date of such sale), any unpaid Basic Rent due through such Basic Rent Payment Date, plus the amount of any deficiency between the Sale Proceeds and Casualty Value, computed as of such Basic Rent Payment Date, together with interest at the interest rate specified in Section 3(b)(iii) on the amount of such Rent and such deficiency from the date of such sale until the date of actual payment;

(vii) in the case of an Event of Default specified in paragraph (iii) of Section 15, the Lessor may demand, by written notice to the Lessee that the Lessee pay to the Lessor, and the Lessee shall pay to the Lessor, on the last Basic Rent Payment Date during the Lease Term, as liquidated damages for loss of a bargain and not as a penalty, any unpaid Rent due through such Basic Rent Payment Date plus an amount (not less than zero) equal to the Fair Market Sales Value of the Undivided Interest and the Real Property Interest (determined on the basis of the then actual condition of Unit 2) determined as of such Basic Rent Payment Date together with interest on such amount at the interest rate specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice to the date of actual payment (and upon receipt of such payment the Lessor shall (or may prior to the receipt of such payment) Transfer to the Lessee the Undivided Interest and the Real Property Interest); provided, however, that the Lessor may not exercise the foregoing remedy if the Lessor shall have failed to Transfer the Undivided Interest and the Real

Property Interest to the bidder (which shall not be the Lessee or an Affiliate of the Lessee or any agent of any thereof) that shall have submitted the highest cash bid on or after the date two years before and on or before the date on which such Event of Default arose, excluding, however, any such cash bid which the Lessor or the Equity Participant determines was not submitted in good faith, or as to which the bidder fails to certify to the Lessor such information as the Lessor or Equity Participant may reasonably request in order to determine whether or not such bid was submitted in good faith (and the Lessor agrees that it will, if and to the extent so requested by the Lessee on or after the date 90 days preceding such last Basic Rent Payment Date, use reasonable efforts (at the expense of the Lessee) to find a Person willing to submit such cash bid; provided, however, that the failure of the Lessor to do so shall not relieve the Lessee of its obligations under this clause (vii)); or

(viii) except in the case of an Event of Default specified in clause (iii) of Section 15, the Lessor may exercise any other right or remedy that may be available to it under any Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(b) No Release. No rescission or termination of this Facility Lease, in whole or in part, or repossession of the Undivided Interest and the Real Property Interest or exercise of any remedy under Section 16(a) shall, except as specifically provided therein, relieve the Lessee of any of its liabilities and obligations hereunder. In addition, the Lessee shall be liable, except as otherwise provided above, for any and all unpaid Rent due hereunder before, after or during the exercise of any of the foregoing remedies, including all reasonable legal fees and other costs and expenses incurred by the Lessor, the Equity Participant or the Indenture Trustee by reason of the occurrence of any Event of Default or the exercise of the Lessor's remedies with respect thereto. At any sale of the Undivided Interest and the Real Property Interest or any part thereof pursuant to this Section 16, the Equity

Participant, the Lessor or the Indenture Trustee may bid for and purchase such property.

(c) Remedies Cumulative. Except as expressly set forth therein, no remedy under Section 16(a) is intended to be exclusive, but each shall be cumulative and in addition to any other remedy provided under Section 16(a) or otherwise available to the Lessor at law or in equity (except that the maximum amount payable by the Lessee in the event of the exercise by the Lessor of any of the remedies provided for in Section 16(a)(v) or (vi) shall not exceed the total amount payable by the Lessee under Section 16(a)(vii) minus the amount provided in subclause (2) of clause (A), (B) or (C) of such Section 16(a)(v), if the Lessor elects a remedy specified in said clause (A), (B) or (C), or the deficiency referred to in Section 16(a)(vi), if the Lessor elects the remedy specified in Section 16(a)(vi) hereof). No express or implied waiver by the Lessor of any Default or Event of Default hereunder shall in any way be, or be construed to be, a waiver of any future or subsequent Default or Event of Default. The failure or delay of the Lessor in exercising any right granted it hereunder upon the occurrence of any of the contingencies set forth herein shall not constitute a waiver of any such right upon the continuation or recurrence of any such contingencies or similar contingencies and any single or partial exercise of any particular right by the Lessor shall not exhaust the same or constitute a waiver of any other right provided herein. To the extent permitted by Applicable Law, the Lessee hereby waives any rights now or hereafter conferred by statute or otherwise which may require the Lessor to sell, lease or otherwise use the Undivided Interest or the Real Property Interest in mitigation of the Lessor's damages as set forth in Section 16(a) or which may otherwise limit or modify any of the Lessor's rights and remedies provided in this Section 16.

(d) Exercise of Other Rights or Remedies. In addition to all other rights and remedies provided in this Section 16, the Lessor may exercise any other right or remedy that may be available to it under Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(e) Special Cure Right of Lessee. If a Notice of Default is given under paragraph (iv) of Section 15,

the Lessee may, on or prior to the occurrence of an Event of Default resulting therefrom, give written notice to the Lessor stating that the Lessee has elected to exercise the option (the Cure Option) provided in this Section 16(e), which election shall be irrevocable as to the Lessee. Promptly after the giving of such notice, the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest and the Real Property Interest or, if they shall be unable so to agree within one month after the date of the Lessee's notice, such value shall be determined by the Appraisal Procedure. On the Basic Rent Payment Date next following the date that such Fair Market Sales Value shall have been determined, the Lessee shall pay to the Lessor all Rent due on such Basic Rent Payment Date, plus an amount equal to the excess of (i) the greater of such Fair Market Sales Value and the Casualty Value determined as of such Basic Rent Payment Date over (ii) the unpaid principal amount of the Notes Outstanding on such date after giving effect to the payment, if any, of the principal installment due and payable and paid in respect of the Notes on such date. If the Lessee shall have made such payment and shall have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture, the Lessor shall Transfer the Undivided Interest to the Lessee. If the Lessee shall have made such payment but shall not have assumed all obligations and liabilities of the Owner Trustee under the Indenture and the Notes pursuant to Section 3.9(b) of the Indenture, the Equity Participant shall effect the Special Transfer, in which case, without further act on the part of the Lessor or the Lessee, (i) the obligation of the Lessee to pay further Basic Rent shall be reduced to an amount payable on each Basic Rent Payment Date thereafter equal to the aggregate amount of principal, premium, if any, and accrued interest then payable on all Notes then Outstanding and (ii) this Facility Lease shall become a security agreement for all purposes of Applicable Law. The Lessee agrees to use its best efforts to comply with the conditions set forth in Section 3.9(b) of the Indenture and, failing such assumption, agrees to accept the Special Transfer.

(f) Offset for Drawings Under Letter of Credit. To the extent there has been an Event of Default under clause (xi) of Section 15 and no Event of Default under any other clause of such Section has occurred and

is continuing, any amount payable in respect of, or with reference to, Casualty Value as provided in this Section shall be reduced by any amount paid under the Letter of Credit in respect of such amount after the occurrence of such Event of Default.

SECTION 17. Notices.

All communications and notices provided for in this Facility Lease shall be in writing and shall be given in person or by means of telex, telecopy, or other wire transmission, or mailed by registered or certified mail, addressed as provided in the Participation Agreement. All such communications and notices given in such manner shall be effective on the date of receipt of such communication or notice.

SECTION 18. Successors and Assigns.

This Facility Lease, including all agreements, covenants, indemnities, representations and warranties, shall be binding upon and inure to the benefit of the Lessor and its successors and permitted assigns, and the Lessee and its successors and, to the extent permitted hereby, assigns.

SECTION 19. Right to Perform for Lessee.

If the Lessee shall fail to make any payment of Rent to be made by it, or shall fail to perform or comply with any of its other agreements contained herein, or shall fail to make any payment to be made by it under any ANPP Project Agreement, or shall fail to perform or comply with any of its other agreements contained in any ANPP Project Agreement, either the Lessor or the Equity Participant may, but shall not be obligated to, (i) to the extent not prohibited by Applicable Law tender such payment, or (ii) to the extent not prohibited by Applicable Law and, in the case of the ANPP Project Agreements, to the extent not expressly prohibited thereby, the ANPP Project Agreements, effect such performance or compliance, and the amount of such payment and the amount of all costs and expenses (including, without limitation, attorneys' and other professionals' fees and expenses) of the Lessor or the Equity Participant, as the case may be, incurred in connection with such payment or the performance of or compliance with such agreement, as the case may be, together with interest thereon at the higher of the

Overdue Interest Rate and the Penalty Rate, shall be deemed Supplemental Rent, payable by the Lessee upon demand. In the event that the Lessor or the Equity Participant shall cure any default by the Lessee under the ANPP Participation Agreement, then (so long as an Event of Default has occurred and is continuing) the Lessor, together with each other Person contributing to such cure, shall be entitled (to the full extent enforceable in accordance with Applicable Law and the ANPP Project Agreements) to receive the Generation Entitlement Share of the Lessee under the ANPP Participation Agreement (not limited to Unit 2); with each contributor to such cure to receive a percentage of such Generation Entitlement Share equal to the percentage of the cure contributed thereby.

SECTION 20. Additional Covenants.

The Lessee agrees to comply with and to pay, as Supplemental Rent, all amounts payable by it under the provisions of Section 13 of the Participation Agreement and the Tax Indemnification Agreement which provisions are incorporated herein by this reference as fully as if set forth in full at this place. The Lessee agrees to comply with its covenants and agreements set forth in Sections 10(b), 14 and 16 of the Participation Agreement and Articles III, IV, V and VI of the Assignment and Assumption, which covenants and agreements are incorporated herein by this reference as fully as if set forth in full at this place.

SECTION 21. Lease of Real Property Interest.

Pursuant to the Deed and the Assignment of Beneficial Interest, the Lessee has sold to the Lessor the Real Property Interest. The Lessor hereby grants to the Lessee a leasehold interest in the Real Property Interest, such leasehold to be coterminous with the lease of the Undivided Interest hereunder and to be at a rent per annum equal to 12% of the Real Estate Investment payable by the Lessee to the Lessor in arrears in equal semiannual installments on each Basic Rent Payment Date during the Lease Term.

SECTION 22. Amendments and Miscellaneous.

(a) Amendments in Writing. The terms of this Facility Lease may not be waived, altered, modified, amended, supplemented or terminated in any manner whatsoever except by written instrument signed by the Lessor and the Lessee.

(b) Survival. (1) All indemnities, representations and warranties contained in this Facility Lease and the other Transaction Documents and any Financing Documents and in any agreement, document or certificate delivered pursuant hereto or thereto or in connection herewith or therewith shall survive, and continue in effect following, the execution and delivery of this Facility Lease and the expiration or other termination of this Facility Lease.

(2) The obligations of the Lessee to pay Supplemental Rent and the obligations of the Lessee under Sections 5, 16, 19 and 20 shall survive the expiration or termination of this Facility Lease. The modification by law of any statute of limitations or the waiver or extension of any statute of limitations by the Owner Trustee, the Indenture Trustee, the Lessee, the Equity Participant, the Loan Participant or any Indemnatee shall not affect such survival. The obligations of the Lessee under Section 20 are expressly made for the benefit of, and shall be enforceable by, any Indemnatee, separately or together, without declaring this Facility Lease to be in default and notwithstanding any assignment by the Lessor of this Facility Lease or any of its rights thereunder or any disposition of all or any part of any interest in the Undivided Interest, the Real Property Interest, Unit 2 or any other property referred to in this Facility Lease or in this Facility Lease or any other Transaction Document or Financing Document. All payments required to be made pursuant to Section 20 shall be made directly to, or as otherwise requested by, the Indemnatee entitled thereto upon written demand by such Indemnatee.

(c) Severability of Provisions. Any provision of this Facility Lease which may be prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof or thereof, and any such prohibition or unenforceability in any jurisdiction

shall not invalidate or render unenforceable such provision in any other jurisdiction. To the extent permitted by Applicable Law, the Lessee hereby waives any provision of law which renders any provision hereof prohibited or unenforceable in any respect.

(d) True Lease. This Facility Lease is intended as and shall constitute an agreement of lease and nothing herein shall be construed as conveying to the Lessee any right, title or interest in or to the Undivided Interest or the Real Property Interest, except as lessee only.

(e) Original Lease. The single executed original of this Facility Lease marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART" and containing the receipt of the Indenture Trustee thereon shall be the Original of this Facility Lease. To the extent that this Facility Lease constitutes chattel paper, as such term is defined in the Uniform Commercial Code as in effect in any applicable jurisdiction, no security interest in this Facility Lease may be created through the transfer or possession of any counterpart other than the Original.

(f) Governing Law. This Facility Lease shall be governed by and construed in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

(g) Headings. The division of this Facility Lease into sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Facility Lease.

(h) Concerning the Owner Trustee. FNB is entering into this Facility Lease solely as Owner Trustee under the Trust Agreement and not in its individual capacity. Anything herein to the contrary notwithstanding, all and each of the representations, warranties, undertakings and agreements herein made on the part of the Owner Trustee are made and intended not as personal representations, warranties, undertakings and agreements by or for the purpose or with the intention of binding FNB personally but are made and intended for the purpose of binding only the Trust Estate, and this Facility Lease is executed and delivered by the Owner Trustee solely in the exercise of the powers expressly

conferred upon it as trustee under the Trust Agreement; and no personal liability or responsibility is assumed hereunder by or shall at any time be enforceable against FNB or any successor in trust or the Equity Participant on account of any representation, warranty, undertaking or agreement hereunder of the Owner Trustee, either expressed or implied, all such personal liability, if any, being expressly waived by the Lessee, except that the Lessee or any Person claiming by, through or under it, making claim hereunder, may look to the Trust Estate for satisfaction of the same and the Owner Trustee or its successor in trust, as applicable, shall be personally liable for its own gross negligence or willful misconduct. If a successor owner trustee is appointed in accordance with the terms of the Trust Agreement, such successor owner trustee shall, without any further act, succeed to all the rights, duties, immunities and obligations of the Owner Trustee hereunder and the predecessor owner trustee shall be released from all further duties and obligations hereunder.

(i) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation, whose address is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

(j) Capacity of Lessee. In addition to being an ANPP Participant, APS is also the Operating Agent for PVNGS. The Lessor understands and agrees that APS has certain duties and responsibilities as such Operating Agent under Applicable Law, as well as to the ANPP Participants under the ANPP Project Agreements, and that the obligations of the Lessee hereunder shall not be interpreted as imposing any additional obligation on APS as a result of its status as Operating Agent.

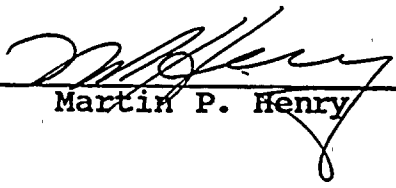
(k) Lien of Lease Indenture. The Lessee hereby agrees that any transfer of all or any part of the property which is subject to the lien of the Indenture, to the extent such lien cannot be released, shall be transferred subject to such lien.

(1) Counterpart Execution. This Facility Lease may be executed in any number of counterparts and by each of the parties hereto or thereto on separate counterparts, all such counterparts together constituting but one and the same instrument.

IN WITNESS WHEREOF, each of the parties hereto has caused this Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation

By


Martin P. Henry

ARIZONA PUBLIC SERVICE
COMPANY

By


Paul A. Williams II

IN WITNESS WHEREOF, each of the parties hereto has caused this Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation

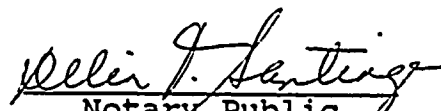
By _____
Martin P. Henry

ARIZONA PUBLIC SERVICE
COMPANY

By  _____
Paul A. Williams II

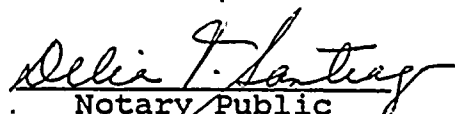
State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by PAUL A. WILLIAMS II, the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of said corporation.


Notary Public
DELIA T. SANTORO
Notary Public, State of New York
No. 41-3451160
Qualified in Queens County
Commission Expires March 30, 1987

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by MARTIN P. HENRY, an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as trustee under that certain Trust Agreement, dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation.


Notary Public
DELIA T. SANTORO
Notary Public, State of New York
No. 41-3451160
Qualified in Queens County
Commission Expires March 30, 1987

When Recorded, Return to: David A. Sprentall
SNELL & WILMER
3100 Valley Bank Center
Phoenix, Arizona 85073

CERTAIN RIGHTS OF THE LESSOR UNDER THE FACILITY LEASE AS AMENDED BY THIS AMENDMENT NO. 1 THERETO HAVE BEEN ASSIGNED TO, AND ARE SUBJECT TO A SECURITY INTEREST IN FAVOR OF, CHEMICAL BANK, AS INDENTURE TRUSTEE UNDER A TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE DATED AS OF AUGUST 1, 1986. THIS AMENDMENT NO. 1 HAS BEEN EXECUTED IN SEVERAL COUNTERPARTS. SEE SECTION 3(d) OF THIS AMENDMENT NO. 1 FOR INFORMATION CONCERNING THE RIGHTS OF HOLDERS OF VARIOUS COUNTERPARTS HEREOF.

THIS COUNTERPART IS NOT THE ORIGINAL COUNTERPART.

AMENDMENT NO. 1
dated as of November 1, 1986

to

FACILITY LEASE
dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON
not in its individual capacity, but solely
as Owner Trustee under a Trust Agreement
dated as of August 1, 1986 with Security
Pacific Capital Leasing Corporation

Lessor

and

ARIZONA PUBLIC SERVICE COMPANY,

Lessee

Original Facility Lease Recorded on August 18, 1986,
as Instrument No. 86-439431 in Maricopa County,
Arizona Recorder's Office.

AMENDMENT NO. 1, dated as of November 1, 1986 (Amendment No. 1), to the Facility Lease dated as of August 1, 1986 between THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement, dated as of August 1, 1986, with Security Pacific Capital Leasing Corporation, a Delaware corporation (the Lessor), and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee).

W I T N E S S E T H :

WHEREAS, the Lessee and the Lessor have heretofore entered into a Facility Lease dated as of August 1, 1986 (the Facility Lease), providing for the lease by the Lessor to the Lessee of the Undivided Interest and the Real Property Interest;

WHEREAS, Section 3(d) of the Facility Lease provides for an adjustment to Basic Rent and to the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event of a Change in Tax Law;

WHEREAS, Section 3(e) of the Facility Lease provides for an adjustment to Basic Rent and to the schedules of Casualty Values, Extraordinary Casualty Values, Special Casualty Values and Modified Special Casualty Values in order to preserve Net Economic Return in the event, among other things, of the refunding, by issuance of the Refunding Notes, of the Initial Series Notes; and

WHEREAS, the Refunding Notes are being issued pursuant to Supplemental Indenture No. 1, dated as of November 1, 1986, to the Indenture;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein and not otherwise defined herein or in the recitals shall have the meanings assigned to such terms in Appendix A hereto.

SECTION 2. Amendments.

(a) The second WHEREAS clause of the Facility Lease is amended hereby by inserting the clause "and the Real Property Interest" in such WHEREAS clause after the first use of the term "Undivided Interest".

(b) Section 3(a)(i) of the Facility Lease is amended hereby to read in its entirety as follows:

"(i) on December 30, 1986, an amount equal to the daily equivalent of Basic Rent (which for the entire period from and including August 18, 1986 to but excluding December 31, 1986, is set forth in Schedule 1 hereto) plus or minus any Rent Differential for the period from the Closing Date to and including December 31, 1986;"

(c) Section 3(a)(ii) of the Facility Lease is amended hereby to read in its entirety as follows:

"(ii) on June 30, 1987 and on each Basic Rent Payment Date thereafter to and including December 30, 2015, an amount equal to the percentage of Facility Cost set forth opposite such Basic Rent Payment Date in Schedule 1 hereto;"

(d) Section 3(a)(iv) of the Facility Lease is amended hereby by replacing the phrase "a Fair Market Renewal Term" with the phrase "the Fair Market Renewal Term" in Section 3(a)(iv).

(e) Section 3(a) of the Facility Lease is amended hereby by amending the clause "such Rent Payment Date" in the penultimate sentence of Section 3(a) to read "such Basic Rent Payment Date" and by amending the last sentence of Section 3(a) in its entirety to read as follows:

"If an interest payment on any Note shall be due on a date other than December 30, 1986 or a Basic Rent Payment Date, the Lessee shall pay Basic Rent on such date equal to such interest payment and such payment of Basic Rent shall be credited against the Basic Rent due on December 30, 1986 or the Basic Rent Payment Date next succeeding the date that such additional Basic Rent shall have been paid."

(f) Section 3(b)(ii) of the Facility Lease is amended hereby by deleting the word "hereunder" from Section 3(b)(ii).

(g) Section 3(e) of the Facility Lease is amended hereby by (i) adding the word "Current" before the phrase "Pricing Assumptions" in the first sentence of Section 3(e) and (ii) by deleting the phrase "hereof also" in the second sentence of Section 3(e).

(h) Section 3(f) of the Facility Lease is amended hereby by (i) replacing the phrase "Sections 3(d) or (e)" with the phrase "Section 3(d) or (e)" in the first sentence of Section 3(f), (ii) replacing the phrase "any Loan Participant" with the phrase "each Loan Participant" in the first sentence of Section 3(f), (iii) replacing the phrase "bank which has issued the Letter of Credit" with the phrase "issuer of the Letter of Credit" in the first sentence of Section 3(f) and (iv) amending the third sentence of Section 3(f) to read in its entirety as follows:

"The revised amounts and percentages, as so confirmed or computed if applicable, shall be conclusive and binding on the Lessee, the Lessor, the Equity Participant, each Loan Participant, the Indenture Trustee and the Collateral Trust Trustee."

(i) Section 3(g) of the Facility Lease is amended hereby by replacing the parenthetical "(when added to all other amounts required to be paid by the Lessee under this Facility Lease in respect of any Event of Loss or Deemed Loss Event or termination of this Facility Lease)" in clause (ii) of Section 3(g) with the parenthetical "(when added to all other amounts required to be paid by the Lessee in respect of any Event of Loss or Deemed Loss Event or purchase by the Lessee of the Undivided Interest or termination of this Facility Lease)".

(j) Section 3(h) of the Facility Lease is hereby amended to read in its entirety as follows:

"(h) Rent Differential. The installment of Basic Rent payable on December 30, 1986 shall be increased or decreased, as the case may be, by the Rent Differential. For purposes hereof, "Rent Differential" shall mean the difference between (i) the aggregate amount of interest paid on the Initial Series Notes and (ii) \$2,285,111.11. If (A) the amount determined in accordance with clause (i) of the immediately preceding sentence shall exceed the amount set forth in clause (ii) of such sentence, the amount of Basic Rent due on such date shall be increased by the Rent Differential, and (B) the amount set forth in such clause (ii) shall exceed the amount determined in accordance with such clause (i), the amount of Basic Rent due on such date shall be decreased by the Rent Differential."

(k) Section 5(a) of the Facility Lease is amended hereby in its entirety to read as follows:

"SECTION 5. Return of the Undivided Interest; Disposition Services.

"(a) Return of the Undivided Interest. Unless the Lessee has acquired the Undivided Interest

and the Real Property Interest as provided herein, on the Lease Termination Date, the Lessee will surrender possession of the Undivided Interest and the Real Property Interest to the Lessor (or to a Person specified by the Lessor to the Lessee in writing not less than 6 months prior to the Lease Termination Date) with full rights as a 'Transferee' and the sole 'Participant' with respect to the Undivided Interest and the Real Property Interest within the meaning of Section 15.10 of the ANPP Participation Agreement, and will furnish to the Lessor: (i) copies certified by a senior officer of the Lessee of all Governmental Actions necessary to effect such surrender (including, without limitation, appropriate amendments to the License permitting the Lessor (without being required to change its business or corporate structure) and for such Person to possess the Undivided Interest and the Real Property Interest without the continued involvement of the Lessee), which Governmental Actions shall be in full force and effect and not subject to any judicial or administrative contest, challenge or review; (ii) if not previously executed and delivered by the Lessee, and if desired by the Lessor, a ground lease covering that portion of the PVNGS Site which is included in the Real Property Interest, which ground lease shall have a term ending on the date of reversion of the Real Property Interest and shall be otherwise reasonably satisfactory to the Lessor, in replacement for the Real Property Interest; and (iii) an opinion of counsel (which may be Mudge Rose Guthrie Alexander & Ferdon, Snell & Wilmer or other counsel experienced in matters pertaining to the Governmental Actions required, reasonably satisfactory to the Equity Participant) to the effect that (A) the Lessee has obtained all Governmental Actions and actions under the ANPP Participation Agreement

necessary to effect such surrender by the Lessee and receipt of possession by the Lessor (or the Person so specified by the Lessor) of the Undivided Interest and the Real Property Interest, (B) the Lessor (or the Person specified by the Lessor) is a NRC Licensee and an ANPP Participant (with all rights and obligations attendant thereto) and no additional Governmental Action will be required in connection with the possession by the Lessor (or the Person specified by the Lessor) of the Undivided Interest and the Real Property Interest, (C) such Governmental Actions are in full force and effect and not subject to any judicial or administrative contest, challenge, or review and (D) to the extent the aforementioned ground lease is required, such ground lease (1) has been duly authorized, executed and delivered, (2) constitutes the legal, valid and binding obligation of the Lessee, (3) does not require the consent of any Person or such consent has been previously received and (4) is not inconsistent with any ANPP Project Agreement. At the time of such return the Lessee shall pay or have paid all amounts due and payable, or to become due and payable, by it as an ANPP Participant under each and every ANPP Project Agreement allocable or chargeable (whether or not payable during or after the Lease Term) to the Undivided Interest or the Real Property Interest in respect of any period or periods ending on or prior to the Lease Termination Date (including, without limitation, all amounts payable with respect to any and all Capital Improvements to Unit 2 or the PVNGS Site approved or authorized (without the concurrence of the Equity Participant) prior to the end of the Lease Term, whether or not implementation thereof has been completed on or prior to the Lease Termination Date), and the Undivided Interest and the Real Property Interest shall be free and clear of all Liens

(other than Permitted Liens described in clauses (i), (v) (other than those for which satisfactory arrangements for the payment thereof have not been made and those arising by, through or under the Lessee alone), (vi), (vii) (other than those arising by, through, or under the Lessee alone), (ix) or (x) of the definition of such term) and in the condition and state of repair required by Section 8. In the event that on or prior to the Lease Termination Date there shall have occurred a default by any ANPP Participant (other than the Lessee) under the ANPP Participation Agreement and such default shall not have been cured by the defaulting ANPP Participant, then (x) the Lessee agrees to indemnify and hold the Lessor (and each successor, assign and transferee thereof) harmless against any and all obligations under the ANPP Participation Agreement with respect to contributions or payments required to be made thereby as a result of such default and (y) the Lessor (and each successor, assign and transferee thereof) agrees to reimburse the Lessee for all amounts paid by the Lessee pursuant to the foregoing clause (x) in respect of the period following the Lease Termination Date to the extent, but only to the extent, that the Lessor (or such successor, assign or transferee) shall have actually received net proceeds from the sale of the Generation Entitlement Share of the defaulting ANPP Participant as a result of the payment made by the Lessee pursuant to the foregoing clause (x), and, to the extent the Lessor (or such successor, assign or transferee) shall have received such proceeds, the amount to be reimbursed to the Lessee pursuant to this clause (y) shall include interest at the Prime Rate from the date of any payment by the Lessee pursuant to the foregoing clause (x) through the date of reimbursement of such amount pursuant to this clause (y)."

(1). Section 8(c) of the Facility Lease is amended hereby by (i) replacing the phrase "The net proceeds" at the beginning of the fourth sentence of Section 8(c) with the phrase "With respect to the net proceeds" and (ii) replacing the seventh sentence of Section 8(c) to read as follows:

"Unless paragraph (3) of Section 8(e) shall be applicable, upon the incorporation of a Capital Improvement in Unit 2, without further act, title to the Unit 2 Interest in such Capital Improvement shall vest in the Lessor and shall become subject to this Facility Lease and be deemed to be part of the Undivided Interest for all purposes hereof to the same extent that the Lessor had a like undivided interest in the property originally incorporated or installed in Unit 2."

(m) Section 9(c) of the Facility Lease is amended hereby by replacing the phrase "On the date next following" in the first sentence of Section 9(c) with the phrase "On a date following".

(n) Section 9(c)(i) of the Facility Lease is amended hereby by (i) replacing the phrase "such ANPP Participant" in Section 9(c)(i) with the phrase "such ANPP Participants", (ii) replacing the phrase "right against the Lessee" in Section 9(c)(i) with the phrase "right against the Lessee)" and (iii) replacing the phrase "may appear);" in Section 9(c)(i) with the phrase "may appear;".

(o) Section 9(g)(ii) is amended hereby by deleting the parenthetical "(ignoring, for this purpose, clause (ii) of the first sentence thereof)".

(p) Section 9(h) of the Facility Lease is amended hereby by amending the clause "or the third sentence of Section 8(c), destruction" to read "or the fourth sentence of Section 8(c), or to any destruction"

and by adding a comma after the phrase "constituting an Event of Loss".

(q) Section 10(a)(1)(i) of the Facility Lease is amended hereby by replacing the first sentence thereof as follows:

"(1) Non-Nuclear Insurance.

"(i) The Lessee shall maintain 'all risk' property insurance covering physical loss with respect to Unit 2 in such amounts and with such other terms as are required by or are in accordance with Prudent Utility Practice, but in no event shall such amounts be less than the estimated maximum probable loss in respect of such property."

(r) Section 10(a)(1)(i)(B) of the Facility Lease is amended to read as follows:

"(B)(i) the Lessor and the Equity Participant (the 'Additional Insureds') are included as additional insureds, as their interests may appear, and (ii) any obligation imposed upon the insured (including without limitation the liability to pay premiums) shall be the sole obligation of the Lessee and not that of any Additional Insured;"

(s) Section 10(a)(1)(ii) of the Facility Lease is amended hereby by adding the phrase "The Lessee shall maintain" immediately after the "(ii)" and before the phrase "bodily injury".

(t) Section 10(a)(2) of the Facility Lease is amended hereby in its entirety to read as follows:

"(2) Nuclear Insurance.

"(i) The Lessee shall maintain nuclear property insurance in amounts and with such other terms as are required by or are in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement and (c) Prudent Utility Practice; provided, however, that such insurance shall at all times be maintained in amounts at least equal to the maximum nuclear property insurance available on commercially reasonable terms. The coverage afforded by such nuclear property insurance in respect of any loss at PVNGS and available for any loss at Unit 2 either (A) shall at all times be at least equal to \$750 million regardless of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of Nuclear Incident) or (B) so long as (1) Unit 2 is in, or is in a procedure which will result in, a state of cold shutdown in accordance with Prudent Utility Practice and (2) the first mortgage bonds of the Lessee shall have an investment grade rating (x) by two nationally accepted rating agencies if such first mortgage bonds are rated by two nationally accepted rating agencies or (y) by one nationally accepted rating agency if such first mortgage bonds are only rated by one nationally accepted rating agency, will be reinstated to be equal to at least \$750 million within 180 days of any suspension, termination, amendment, supplement or reduction of such insurance for any reason (including by reason of a Nuclear Incident). Such insurance may include deductible amounts not to exceed \$10,000,000. Any insurance carried in accordance with this Section 10(a)(2)(i) shall be endorsed by the insurer as provided in paragraphs (A), (B), (D), (E) and (F) of Section 10(a)(1)(i).

"(ii) The Lessee shall maintain the maximum nuclear liability insurance in amounts

and with such other terms as are required by or in accordance with the highest of (a) Applicable Law, (b) the ANPP Participation Agreement, (c) Prudent Utility Practice and (d) the maximum nuclear liability insurance available on commercially reasonable terms, but in any event in such amounts and containing such other terms as to cover the 'aggregate liability' for a single 'nuclear incident' of all 'persons indemnified' (as such terms are used in the Atomic Energy Act) and in connection with the ownership, maintenance, condition or use of Unit 2 and the PVNGS Site. The Lessee shall also maintain supplier's and transporter's insurance in amounts consistent with Prudent Utility Practice. The Lessee shall maintain nuclear liability insurance pursuant to this Section 10(a)(2)(ii), whether or not the Lease Termination Date shall have occurred, until notified by the Equity Participant that neither the Lessor nor the Equity Participant has any further real or potential liability in connection with the ownership, operation, maintenance, condition or use of Unit 2 or the PVNGS Site; provided that after Decommissioning has been completed the Lessee shall not be required to maintain nuclear liability insurance for more than 30 years. Any insurance carried in accordance with this Section 10(a)(2)(ii) shall be endorsed as provided in paragraphs (B), (D), (E) and (F) of Section 10(a)(1)(i).

"(iii) The Lessee shall, or shall cause the Operating Agent to, use its best efforts at all times to obtain the endorsement referred to in paragraph (C) of Section 10(a)(1)(i) on all insurance referred to in this Section 10(a)(2), and shall cause such endorsement to be obtained if and to the extent it is available to any other owner or operator of a nuclear generating unit."

(u) Section 11(b) of the Facility Lease is hereby amended by amending the last sentence of Section 11(b) in its entirety to read as follows:

"Following any transfer to, or purchase by, Lessee of the Undivided Interest and the Real Property Interest, the Undivided Interest and the Real Property Interest shall (unless the Notes shall have been paid in full) remain subject to the lien of the Indenture and such lien shall not be impaired in consequence thereof."

(v) Section 12(b) of the Facility Lease is amended hereby in its entirety to read as follows:

"(b) Fair Market Renewal Term. Subject to the notice requirements set forth in Section 13(b), at the expiration of the Fixed Rate Renewal Term (including any extension thereof pursuant to Section 12(a)(ii)) elected by the Lessee under paragraph (a) of this Section 12, and provided that no Default or Event of Default shall have occurred and be continuing hereunder, no Event of Loss or Deemed Loss Event shall have occurred and all Notes shall have been paid in full, the Lessee may renew the term of this Facility Lease for a period of 6, 12, 18 or 24 months (herein referred to as the Fair Market Renewal Term; and the Fixed Rate Renewal Term (including any extension thereof) and the Fair Market Renewal Term each herein referred to as a Renewal Term), in which case Basic Rent payable during such Fair Market Renewal Term shall be as set forth in Section 3(a)(iv)."

(w) Section 13(a) of the Facility Lease is amended hereby in its entirety to read as follows:

"(a) Expiration of Basic Lease Term. Not earlier than five nor later than three years prior to the expiration date of the Basic Lease Term, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(a) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration date of the Basic Lease Term, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fixed Rate Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor if, on the effective date thereof, a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(a), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such Fair Market Sales Value shall be determined by the Appraisal Procedure. In the case of the exercise of the option for the Fixed Rate Renewal Term, the Maximum Option Period shall be determined by the Appraisal Procedure."

(x). Section 13(b) of the Facility Lease is amended hereby in its entirety to read as follows:

"Expiration of Fixed Rate Renewal Term. Not earlier than five years nor later than three years prior to the expiration date of the Fixed Rate Renewal Term, if elected, the Lessee shall give to the Lessor written notice (which shall be irrevocable except as provided in Section 10(b)(3)(xiii) of the Participation Agreement) of its election either to (1) return the Undivided Interest and the Real Property Interest to the Lessor pursuant to Section 5 or (2) exercise the renewal option permitted by Section 12(b) or the purchase option permitted by Section 13(c). If the notice specified in clause (2) of the preceding sentence is given, then not later than 18 months prior to the expiration of the Fixed Rate Renewal Term, the Lessee will give the Lessor written notice of its election to exercise either (x) the purchase option permitted by Section 13(c) or (y) the option to renew this Facility Lease for the Fair Market Renewal Term. Any such election shall be irrevocable as to the Lessee, but no such election shall be binding on the Lessor, if, on the effective date thereof, a Default or an Event of Default shall have occurred and be continuing or an Event of Loss or Deemed Loss Event shall have occurred. Promptly after giving the notice pursuant to clause (2) of the first sentence of this Section 13(b), the Lessee and the Equity Participant shall agree upon the Fair Market Sales Value and the Fair Market Rental Value of the Undivided Interest and the Real Property Interest. If within three months after the date of the Lessee's notice, the Lessee and the Equity Participant shall be unable so to agree, such values shall be determined by the Appraisal Procedure."

(y) Section 13(c) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 13(c).

(z) Section 13(d) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in the heading and after the first use of the phrase "Undivided Interest" in the first sentence of Section 13(d).

(aa) Section 13(e) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 13(e).

(bb) Section 14(c) of the Facility Lease is amended hereby by (i) adding the phrase "and the Real Property Interest" after the two uses of the phrase "Undivided Interest" in the first sentence of Section 14(c), (ii) amending the second and third sentences of Section 14(c) in their entirety to read as follows:

"The total sale price realized at such sale shall be retained by the Lessor (subject, however, to the terms of the Indenture and the requirement that on the Termination Date there shall have been paid, or provision for payment made, to the Indenture Trustee the unpaid principal amount of all Notes Outstanding on the Obsolescence Redemption Date and all premium, if any, and interest accrued and unpaid on such Outstanding Notes as of the Termination Date, and to accrue on such Outstanding Notes to the Obsolescence Redemption Date) and, in addition, on the Termination Date the Lessee shall pay to the Lessor (A) the excess, if any, of the sum of the Special Casualty Value as of the Termination Date over the net sale price of the Undivided Interest and the Real Property Interest and (B) any Basic Rent due or

accrued, as the case may be, to and including the Termination Date and an amount equal to any interest to accrue on the Outstanding Notes from and including the Termination Date to the Obsolescence Redemption Date and shall pay to the Person or Persons entitled thereto all Supplemental Rent (other than Special Casualty Value). Upon compliance by the Lessee with the applicable provisions of this Section 14, the obligation of the Lessee to pay Basic Rent for any period after the Termination Date shall cease and the Basic Lease Terms shall end on the Termination Date but the obligation of the Lessee to pay Supplemental Rent when and as due shall continue in full force and effect and shall not be impaired by reason of any such termination."

and (iii) by adding the phrase "and the Real Property Interest" after the first use of the phrase "Undivided Interest" in the last sentence of Section 14(c).

(cc) Section 15(xi) of the Facility Lease is amended hereby by replacing the term "Lessor" with the term "Equity Participant" each time such term is used in Section 15(xi).

(dd) Section 16(a)(v) of the Facility Lease is amended hereby by (i) replacing the phrase "proviso to" with the phrase "parenthetical in" in the first parenthetical clause of Section 16(a)(v), (ii) removing the parenthesis before the colon in the first paragraph of Section 16(a)(v), and (iii) adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in Section 16(v)(A).

(ee) Section 16(a)(vii) of the Facility Lease is amended hereby by replacing the clause "specified in Section 3(b)(iii) from the Basic Rent Payment Date specified in such notice" in Section 16(a)(vii) with the clause "specified in Section 3(b)(iii) from such last Basic Rent Payment Date".

(ff) Section 16(c) of the Facility Lease is amended hereby by amending the first sentence of Section 16(c) in its entirety to read as follows:

"Except as expressly set forth therein, no remedy under Section 16(a) is intended to be exclusive, but each shall be cumulative and in addition to any other remedy provided under Section 16(a) or otherwise available to the Lessor at law or in equity (except that, in the case of an Event of Default specified in clause (iii) of Section 15, the Lessor may not exercise any of the remedies provided for in Section 16(a)(v), 16(a)(vi) or 16(a)(viii))."

(gg) Section 16(e) of the Facility Lease is amended hereby by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest" in the fourth sentence of Section 16(e) and by deleting the last sentence of Section 16(e).

(hh) Section 21 of the Facility Lease is amended hereby by deleting the phrase "and the Assignment of Beneficial Interest" from Section 21.

(ii) Section 22(b)(2) of the Facility Lease is amended hereby by replacing the phrase "the Loan Participant" in the second sentence of Section 22(b)(2) with the phrase "any Loan Participant".

(jj) The Facility Lease is amended hereby by replacing the phrase "any Collateral Trust Trustee" with the phrase "the Collateral Trust Trustee" in each place in the Facility Lease where such phrase appears.

(kk) Appendix A to the Facility Lease is hereby deleted in its entirety and replaced with Appendix A hereto.

(ll) Schedule 1 to the Facility Lease is hereby replaced with Schedule 1 hereto.

(mm) Schedule 2 to the Facility Lease is hereby replaced with Schedule 2 hereto.

(nn) Schedule 3 to the Facility Lease is hereby replaced with Schedule 3 hereto.

(oo) Schedule 4 to the Facility Lease is hereby replaced with Schedule 4 hereto.

(pp) Schedule 5 to the Facility Lease is hereby replaced with Schedule 5 hereto.

(qq) The titles of Schedules 6 and 7 to the Facility Lease are hereby changed to "Description of Undivided Interest" and "Description of Real Property Interest", respectively.

(rr) Schedule 8 to the Facility Lease is hereby deleted.

SECTION 3. Miscellaneous.

(a) Dating. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Governing Law. This Amendment No. 1 has been negotiated and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York, except to the extent that pursuant to the law of the State of Arizona such law is mandatorily applicable hereto.

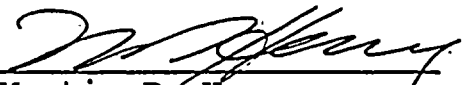
(c) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation. The address of the beneficiary is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust

Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

(d) Original Counterpart. The single executed original of this Amendment No. 1 marked "THIS COUNTERPART IS THE ORIGINAL COUNTERPART" and containing the receipt of the Indenture Trustee thereon shall be the "Original" of this Amendment No. 1. No security interest in this Amendment No. 1 may be created or continued through the transfer or possession of any counterpart other than the "Original".


IN WITNESS WHEREOF, each of the parties hereto has caused this Amendment No. 1 to Facility Lease to be duly executed in New York, New York by an officer thereunto duly authorized.

THE FIRST NATIONAL BANK OF
BOSTON,
not in its individual
capacity, but solely as
Owner Trustee under a Trust
Agreement dated as of
August 1, 1986, with
Security Pacific Capital
Leasing Corporation

By 
Martin P. Henry
Assistant Vice President

Date: November 19, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By 
Paul A. Williams II
Vice President and Treasurer

Date: November 19, 1986

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under the Trust Agreement dated as of August 1, 1986 with Security Pacific Capital Leasing Corporation.

Anita Rubin
Notary Public
ANITA RUBIN
Notary Public, State of New York
No. 03-317529
Qualified in Bronx County
Commission Expires ~~March 30, 1988~~
June 88

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by PAUL A. WILLIAMS II, Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.

Anita Rubin
Notary Public
ANITA RUBIN
Notary Public, State of New York
No. 03-317529
Qualified in Bronx County
Commission Expires ~~March 30, 1988~~
June 88

SCHEDULE 1
to
AMENDMENT NO. 1

BASIC RENT PERCENTAGES

Basic Rent Payment Date	Basic Rent Number	% of Facility Cost	Basic Rent Payment Date	Basic Rent Number	% of Facility Cost
12 /30 /1986	0	3.6550925	12 /30 /2001	30	5.3354538
6 /30 /1987	1	4.3653713	6 /30 /2002	31	5.3354538
12 /30 /1987	2	4.3653713	12 /30 /2002	32	5.3354538
6 /30 /1988	3	4.3653713	6 /30 /2003	33	5.3354538
12 /30 /1988	4	4.3653713	12 /30 /2003	34	5.3354538
6 /30 /1989	5	4.3653713	6 /30 /2004	35	5.3354538
12 /30 /1989	6	4.3653713	12 /30 /2004	36	5.3354538
6 /30 /1990	7	4.3653713	6 /30 /2005	37	5.3354538
12 /30 /1990	8	4.3653713	12 /30 /2005	38	5.3354538
6 /30 /1991	9	4.3653713	6 /30 /2006	39	5.3354538
12 /30 /1991	10	4.3653713	12 /30 /2006	40	5.3354538
6 /30 /1992	11	4.3653713	6 /30 /2007	41	5.3354538
12 /30 /1992	12	4.3653713	12 /30 /2007	42	5.3354538
6 /30 /1993	13	4.3653713	6 /30 /2008	43	5.3354538
12 /30 /1993	14	4.3653713	12 /30 /2008	44	5.3354538
6 /30 /1994	15	4.3653713	6 /30 /2009	45	5.3354538
12 /30 /1994	16	4.3653713	12 /30 /2009	46	5.3354538
6 /30 /1995	17	4.3653713	6 /30 /2010	47	5.3354538
12 /30 /1995	18	4.3653713	12 /30 /2010	48	5.3354538
6 /30 /1996	19	4.3653713	6 /30 /2011	49	5.3354538
12 /30 /1996	20	4.3653713	12 /30 /2011	50	5.3354538
6 /30 /1997	21	4.3653713	6 /30 /2012	51	5.3354538
12 /30 /1997	22	5.3354538	12 /30 /2012	52	5.3354538
6 /30 /1998	23	5.3354538	6 /30 /2013	53	5.3354538
12 /30 /1998	24	5.3354538	12 /30 /2013	54	5.3354538
6 /30 /1999	25	5.3354538	6 /30 /2014	55	5.3354538
12 /30 /1999	26	5.3354538	12 /30 /2014	56	5.3354538
6 /30 /2000	27	5.3354538	6 /30 /2015	57	5.3354538
12 /30 /2000	28	5.3354538	12 /30 /2015	58	5.3354538
6 /30 /2001	29	5.3354538			

SCHEDULE 2
to
AMENDMENT NO. 1

CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Basic Rent Payment Date	Casualty Value
6 /30 /1987	105.0471076
and before	
12 /30 /1987	107.4393145
6 /30 /1988	106.7767733
12 /30 /1988	108.5345577
6 /30 /1989	110.1269395
12 /30 /1989	111.5781223
6 /30 /1990	112.8850447
12 /30 /1990	114.0580202
6 /30 /1991	115.0868190
12 /30 /1991	115.9612471
6 /30 /1992	116.6733631
12 /30 /1992	117.2300211
6 /30 /1993	117.6214061
12 /30 /1993	117.8354629
6 /30 /1994	117.8582291
12 /30 /1994	117.6745246
6 /30 /1995	117.3570364
12 /30 /1995	116.9780893
6 /30 /1996	116.5463951
12 /30 /1996	116.0969732
6 /30 /1997	115.6335250
12 /30 /1997	114.1877760
6 /30 /1998	112.6950687
12 /30 /1998	111.1548999
6 /30 /1999	109.5657747
12 /30 /1999	107.9139873
6 /30 /2000	106.1968996
12 /30 /2000	104.4117541
6 /30 /2001	102.5557713

Basic Rent Payment Date	Casualty Value
12 /30 /2001	100.6462825
6 /30 /2002	98.6761302
12 /30 /2002	96.6437504
6 /30 /2003	94.5475850
12 /30 /2003	92.3860481
6 /30 /2004	90.1597769
12 /30 /2004	87.8696021
6 /30 /2005	85.5150427
12 /30 /2005	83.0954052
6 /30 /2006	80.6092769
12 /30 /2006	78.0551281
6 /30 /2007	75.4313965
12 /30 /2007	72.7365363
6 /30 /2008	69.9689653
12 /30 /2008	67.1271137
6 /30 /2009	64.2093703
12 /30 /2009	61.2141313
6 /30 /2010	58.1397983
12 /30 /2010	54.9847777
6 /30 /2011	51.7474262
12 /30 /2011	48.4261504
6 /30 /2012	45.0193560
12 /30 /2012	41.5254454
6 /30 /2013	37.9428152
12 /30 /2013	34.3351307
6 /30 /2014	30.6837740
12 /30 /2014	27.1329778
6 /30 /2015	23.7130963
12 /30 /2015	20.0000000

SCHEDULE 3
to
AMENDMENT NO. 1

SPECIAL CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Basic Rent Payment Date	Special Casualty Value	Basic Rent Payment Date	Special Casualty Value
6 /30 /1987	104.6404760		
and before			
12 /30 /1987	107.0091832	12 /30 /2001	98.5723218
6 /30 /1988	106.3217841	6 /30 /2002	96.4823126
12 /30 /1988	108.0532741	12 /30 /2002	94.3231493
6 /30 /1989	109.6178420	6 /30 /2003	92.0928734
12 /30 /1989	111.0396034	12 /30 /2003	89.7894755
6 /30 /1990	112.3154041	6 /30 /2004	87.4131451
12 /30 /1990	113.4554593	12 /30 /2004	84.9642390
6 /30 /1991	114.4494354	6 /30 /2005	82.4417750
12 /30 /1991	115.2870282	12 /30 /2005	79.8445294
6 /30 /1992	115.9601803	6 /30 /2006	77.1705288
12 /30 /1992	116.4756225	12 /30 /2006	74.4176503
6 /30 /1993	116.8234098	6 /30 /2007	71.5837043
12 /30 /1993	116.9913494	12 /30 /2007	68.6664810
6 /30 /1994	116.9653332	6 /30 /2008	65.6636964
12 /30 /1994	116.7300271	12 /30 /2008	62.5730378
6 /30 /1995	116.3579552	6 /30 /2009	59.3921086
12 /30 /1995	115.9212699	12 /30 /2009	56.1184738
6 /30 /1996	115.4285008	6 /30 /2010	52.7496563
12 /30 /1996	114.9144744	12 /30 /2010	49.2831325
6 /30 /1997	114.3826881	6 /30 /2011	45.7162756
12 /30 /1997	112.8646516	12 /30 /2011	42.0464519
6 /30 /1998	111.2954792	6 /30 /2012	38.2709666
12 /30 /1998	109.6744263	12 /30 /2012	34.3870580
6 /30 /1999	107.9997427	6 /30 /2013	30.3918913
12 /30 /1999	106.2574524	12 /30 /2013	26.3478293
6 /30 /2000	104.4446314	6 /30 /2014	22.2348762
12 /30 /2000	102.5582201	12 /30 /2014	18.1958074
6 /30 /2001	100.5951192	6 /30 /2015	14.2594355
		12 /30 /2015	10.0000000

SCHEDULE 4
to
AMENDMENT NO. 1

MODIFIED SPECIAL CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Date	Modified Special Casualty Value	Date	Modified Special Casualty Value
-----	-----	-----	-----
6 /30 /1987 and before	104.2338445	12 /30 /2001	96.4983610
12 /30 /1987	106.5790519	6 /30 /2002	94.2884950
6 /30 /1988	105.8667950	12 /30 /2002	92.0025482
12 /30 /1988	107.5719905	6 /30 /2003	89.6381618
6 /30 /1989	109.1087444	12 /30 /2003	87.1929030
12 /30 /1989	110.5010844	6 /30 /2004	84.6665134
6 /30 /1990	111.7457634	12 /30 /2004	82.0588759
12 /30 /1990	112.8528984	6 /30 /2005	79.3685072
6 /30 /1991	113.8120517	12 /30 /2005	76.5936536
12 /30 /1991	114.6128093	6 /30 /2006	73.7317807
6 /30 /1992	115.2469974	12 /30 /2006	70.7801726
12 /30 /1992	115.7212240	6 /30 /2007	67.7360121
6 /30 /1993	116.0254136	12 /30 /2007	64.5964258
12 /30 /1993	116.1472359	6 /30 /2008	61.3584275
6 /30 /1994	116.0724373	12 /30 /2008	58.0189619
12 /30 /1994	115.7855296	6 /30 /2009	54.5748468
6 /30 /1995	115.3588741	12 /30 /2009	51.0228163
12 /30 /1995	114.8644505	6 /30 /2010	47.3595142
6 /30 /1996	114.3106065	12 /30 /2010	43.5814873
12 /30 /1996	113.7319756	6 /30 /2011	39.6851250
6 /30 /1997	113.1318511	12 /30 /2011	35.6667535
12 /30 /1997	111.5415271	6 /30 /2012	31.5225773
6 /30 /1998	109.8958898	12 /30 /2012	27.2486706
12 /30 /1998	108.1939528	6 /30 /2013	22.8409673
6 /30 /1999	106.4337108	12 /30 /2013	18.3605278
12 /30 /1999	104.6009174	6 /30 /2014	13.7859784
6 /30 /2000	102.6923631	12 /30 /2014	9.2586370
12 /30 /2000	100.7046860	6 /30 /2015	4.8057746
6 /30 /2001	98.6344670	12 /30 /2015	0.0000000

SCHEDULE 5
to
AMENDMENT NO. 1

EXTRAORDINARY CASUALTY VALUES
(Expressed as Percentage of Facility Cost)

Date	Extraordinary Casualty Value	Date	Extraordinary Casualty Value
-----	-----	-----	-----
6 /30 /1987	105.2504234	12 /30 /2001	101.6832629
12 /30 /1987	107.6543802	6 /30 /2002	99.7730390
6 /30 /1988	107.0042679	12 /30 /2002	97.8040510
12 /30 /1988	108.7751994	6 /30 /2003	95.7749408
6 /30 /1989	110.3814883	12 /30 /2003	93.6843343
12 /30 /1989	111.8473818	6 /30 /2004	91.5330927
6 /30 /1990	113.1698650	12 /30 /2004	89.3222837
12 /30 /1990	114.3593007	6 /30 /2005	87.0516766
6 /30 /1991	115.4055109	12 /30 /2005	84.7208431
12 /30 /1991	116.2983565	6 /30 /2006	82.3286509
6 /30 /1992	117.0299545	12 /30 /2006	79.8738669
12 /30 /1992	117.6072204	6 /30 /2007	77.3552426
6 /30 /1993	118.0204042	12 /30 /2007	74.7715639
12 /30 /1993	118.2575196	6 /30 /2008	72.1215998
6 /30 /1994	118.3046770	12 /30 /2008	69.4041516
12 /30 /1994	118.1467733	6 /30 /2009	66.6180012
6 /30 /1995	117.8565770	12 /30 /2009	63.7619600
12 /30 /1995	117.5064989	6 /30 /2010	60.8348693
6 /30 /1996	117.1053423	12 /30 /2010	57.8356003
12 /30 /1996	116.6882226	6 /30 /2011	54.7630015
6 /30 /1997	116.2589435	12 /30 /2011	51.6159996
12 /30 /1997	114.8493382	6 /30 /2012	48.3935507
6 /30 /1998	113.3948634	12 /30 /2012	45.0946391
12 /30 /1998	111.8951366	6 /30 /2013	41.7182772
6 /30 /1999	110.3487907	12 /30 /2013	38.3287815
12 /30 /1999	108.7422548	6 /30 /2014	34.9082229
6 /30 /2000	107.0730337	12 /30 /2014	31.6015629
12 /30 /2000	105.3385211	6 /30 /2015	28.4399268
6 /30 /2001	103.5360974	12 /30 /2015	25.0000000

TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND
ASSIGNMENT OF FACILITY LEASE

Dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON, not
in its individual capacity, but solely
as Owner Trustee under a Trust
Agreement dated as of August 1,
1986, with SECURITY PACIFIC
CAPITAL LEASING CORPORATION

and

CHEMICAL BANK,
as Indenture Trustee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

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TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE dated as of August 1, 1986, between THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as trustee under a Trust Agreement dated as of August 1, 1986 between FNB, whose address is 100 Federal Street, Boston, Massachusetts 02110, with Security Pacific Capital Leasing Corporation, and CHEMICAL BANK, a New York banking corporation, whose address is 55 Water Street, New York, New York 10041.

W I T N E S S E T H:

WHEREAS, the Owner Trustee has entered into a Participation Agreement, dated as of August 1, 1986 among the Equity Participant, PVNGS Funding Corp., Inc., a Delaware corporation, Bank of America National Trust and Savings Association, a national banking association, Arizona Public Service Company, an Arizona corporation, and the Indenture Trustee;

WHEREAS, the Owner Trustee, acting on behalf of the Equity Participant, pursuant to the Trust Agreement and the Participation Agreement, intends to purchase the Undivided Interest and the Real Property Interest from APS and lease the Undivided Interest and the Real Property Interest to APS pursuant to the Facility Lease;

WHEREAS, in order to finance a portion of the Purchase Price of the Undivided Interest, the Owner Trustee desires to issue its promissory notes hereunder with such promissory notes to be substantially in the form of Exhibit A hereto;

WHEREAS, in the circumstances contemplated by Sections 2(d) and 2(e) of the Participation Agreement, the Owner Trustee may desire to issue Refunding Notes (together with any other Notes issued hereunder other than the Initial Series Notes, the Additional Notes) or to increase the principal amount of the Outstanding Refunding Notes or to change the amortization of either or both thereof;

WHEREAS, in order to finance the Supplemental Financing Amount of Capital Improvements and to refund notes of any series previously issued, the Owner Trustee may desire to issue additional Refunding Notes hereunder secured on a pari passu basis with other Notes Outstanding from time to time;

WHEREAS, in order to secure the obligations referred to herein, the Owner Trustee desires to grant to the Indenture Trustee the security interest and realty mortgage herein provided and the parties hereto desire that this Indenture be regarded (i) as a "security agreement" and as a "financing statement" for such security agreement under the Uniform Commercial Code and (ii) to the extent that the Undivided Interest and the Real Property Interest constitute fixtures or real property, as a realty mortgage;

NOW, THEREFORE, in consideration of the premises, of the acceptance by the Indenture Trustee of the trusts hereby created and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

CONSTRUCTION, GOVERNING LAW, INTERPRETATION AND DEFINITIONS

SECTION 1.1. Governing Law.

This Indenture (i) is being executed and delivered in the State of New York, (ii) shall be deemed to be a contract made in such State and (iii) for all purposes shall be construed in accordance with and governed by the laws of the State of New York, except to the extent to which the laws of the State of Arizona are mandatorily applicable hereto.

SECTION 1.2. Headings and Table of Contents.

The division of this Indenture into articles and sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Indenture.

SECTION 1.3. Definitions; Construction of References.

In this Indenture, unless the context otherwise requires:

(a) the term this Indenture means this instrument together with all exhibits, appendices and schedules hereto as originally executed and as it may from time to time be supplemented or amended by one or more indentures supplemental hereto pursuant to the provisions hereof;

(b) all references in this instrument to designated Articles, Sections and other subdivisions are to designated Articles, Sections and other subdivisions of this instrument unless otherwise indicated;

(c) all accounting terms not otherwise defined herein shall have the meanings assigned to them in accordance with generally accepted accounting principles; and

(d) capitalized terms used herein which are not otherwise defined herein shall have the meanings set forth in Appendix A hereto (as such Appendix may be supplemented or amended pursuant to, and in accordance with, the terms hereof), and the rules of construction set forth in Appendix A hereto shall be applicable hereto.

SECTION 1.4. Disclosure of Beneficiaries.

Pursuant to Arizona Revised Statutes Section 33-401, (i) the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation, whose address is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV and (ii) the beneficiary of this Indenture is (1) during the period that the Initial Series Notes are Outstanding, the Agent, whose address is 555 South Flower Street, Los Angeles, California 90071, (2) during the period that the Loan Participant is the Funding Corp, PVNGS Funding Corp., Inc., whose address is Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 19801, Attention: President and, by pledge and assignment, Chemical Bank, as trustee under the Collateral Trust Indenture, whose address is 55 Water Street, New York, New York 10041: Attention of Corporate Trustee Administration and (3) during any period that the Loan Participant is other than the Agent or the Funding Corp, at the address set forth in the applicable indenture supplemental to this Indenture. Copies of the Trust Agreement and this Indenture are

available for inspection at the Indenture Trustee's Office.

ARTICLE II

SECURITY

SECTION 2.1. Grant of Security Interest; Mortgage.

As security for the due and punctual payment of the principal of and premium, if any, and interest on the Notes according to their respective terms and effect and the performance and observance by the Owner Trustee of all the covenants and agreements made by it or on its behalf in the Notes, the Participation Agreement and this Indenture, the Owner Trustee does by its execution and delivery hereof hereby grant a security interest in and grant, bargain, convey, warrant, assign, transfer, mortgage, pledge and set over unto the Indenture Trustee, and to its successors and assigns in trust, for the ratable benefit of the Holders of the Notes, the following (the Lease Indenture Estate):

(1) all right, title and interest of the Owner Trustee in and to the Undivided Interest and the Real Property Interest;

(2) all right, title and interest of the Owner Trustee in, to and under (a) the Purchase Documents, (b) the ANPP Participation Agreement, (c) the Assignment and Assumption Agreement and (d) the Facility Lease (collectively the Granting Clause Documents), and all sums payable to the Owner Trustee with respect thereto, including, without limitation, (x) all amounts of Rent (including, without limitation, Basic Rent and Supplemental Rent) and payments under and pursuant to Sections 13(c) and 16 of the Facility Lease (the Assigned Payments), insurance proceeds and condemnation, requisition and other awards and payments of any kind for or with respect to any part of the Lease Indenture Estate as contemplated in or by the Granting Clause Documents and (y) all rights of the Owner Trustee to exercise any election or

option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of any Granting Clause Document, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under any Granting Clause Document or by statute or at law or equity or otherwise, arising out of any Indenture Event of Default;

(3) all moneys and securities deposited or required to be deposited with the Indenture Trustee pursuant to any term of this Indenture and held or required to be held by the Indenture Trustee hereunder;

(4) all rents (including Rent), issues, profits, products, revenues and other income of all property from time to time subjected to the lien of this Indenture, and all right, title and interest of every nature whatsoever of the Owner Trustee in and to the same and every part thereof; and

(5) all proceeds of the foregoing;

BUT EXCLUDING from the Lease Indenture Estate any and all Excepted Payments and Excepted Rights; and SUBJECT, HOWEVER, TO (i) the terms and provisions of this Indenture and (ii) the rights of the Lessee under the Facility Lease.

To the extent that any portion of the Lease Indenture Estate constitutes fixtures or real property, this Indenture constitutes a realty mortgage and an assignment of rents with respect to all such items of real property and, in addition to all other rights or remedies set forth in this Indenture, the Indenture Trustee shall have, to the extent not inconsistent with this Indenture, all of the rights, remedies and benefits of a mortgagee of real property under Applicable Law, including, without limitation, the rights and remedies pursuant to Arizona Revised Statutes, Section 33-702.B, and the Owner Trustee shall be deemed a mortgagor with respect to such items.

Concurrently with the delivery hereof, the Owner Trustee is delivering to the Indenture Trustee the executed original counterpart of the Facility Lease and

the Assignment and Assumption (which the Indenture Trustee will at all times maintain possession of).

TO HAVE AND TO HOLD all the Lease Indenture Estate unto the Indenture Trustee, its successors and assigns FOREVER, BUT IN TRUST, NEVERTHELESS, for the ratable benefit and security of the Holders of the Notes without priority of any one Note over the other except as herein otherwise expressly provided, and for the uses and purposes and subject to the terms and conditions set forth in this Indenture.

UPON CONDITION that, unless and until an Indenture Event of Default shall have occurred and be continuing, the Owner Trustee shall be permitted, to the exclusion of the Indenture Trustee, but subject to the provisions hereof, including, without limitation, Sections 6.11 and 10.2, to possess and use the Lease Indenture Estate and exercise all rights with respect thereto and, without limitation of the foregoing, the Owner Trustee may exercise all of its rights under the Granting Clause Documents to the same extent as if its right, title and interest therein had not been assigned to the Indenture Trustee, except that the Indenture Trustee shall receive all payments of Assigned Payments and all moneys and securities required to be held by or deposited with the Indenture Trustee hereunder.

It is expressly agreed that, anything herein contained to the contrary notwithstanding, the Owner Trustee shall remain obligated under the Granting Clause Documents to perform all of the Owner Trustee's obligations thereunder in accordance with the terms and provisions thereof, and the Indenture Trustee shall not be required or obligated in any manner, except as expressly provided herein, to perform or fulfill any obligations of the Owner Trustee under any Granting Clause Document or to make any payment, or to make any inquiry as to the nature or sufficiency of any payment received by it, or to present or file any claim, or to take any action to collect or enforce the payment of any amounts or otherwise to protect or preserve any rights which may have been assigned to it or to which it may be entitled at any time or times.

The Owner Trustee hereby warrants and represents that it has not assigned or pledged any of its right, title or interest in and to the Lease Indenture Estate to anyone other than the Indenture Trustee or otherwise granted or created any right prior to or

inconsistent with the rights of the Indenture Trustee under this Indenture.

SECTION 2.2. Payments Under Granting Clause Documents.

Until release of the lien of the Lease Indenture Estate, all payments due or to become due under any Granting Clause Document to the Owner Trustee (except so much of such payments as constitute Excepted Payments) shall be made directly to the Indenture Trustee or in accordance with the Indenture Trustee's instructions. The Owner Trustee agrees that if it should receive any such payments to be made to the Indenture Trustee or any proceeds for or with respect to the Lease Indenture Estate or as a result of the sale or other disposition thereof or otherwise constituting part of the Lease Indenture Estate to which the Owner Trustee is not entitled hereunder, it will promptly forward such payments to the Indenture Trustee or in accordance with the Indenture Trustee's instructions. The Indenture Trustee agrees to apply payments from time to time received by it (from the Lessee, the Owner Trustee or otherwise) with respect to the Lease Indenture Estate in the manner provided in Section 3.11 and Article V.

SECTION 2.3. Release of Security Interest in Undivided Interest and Real Property Interest.

In case a release from the security and other interests created by Section 2.1 by the Indenture Trustee of a portion of the Lease Indenture Estate shall be necessary in order to enable the Lessee to perform its covenants and agreements set forth in Section 10(b)(2) of the Participation Agreement or the Owner Trustee or the Lessee to carry out any action required by Section 8 of the Facility Lease, the Indenture Trustee shall execute and deliver to, or as directed by, the Owner Trustee an appropriate instrument or instruments provided to the Indenture Trustee by the Owner Trustee or the Lessee (in due form for filing or recording), so releasing a portion of the Lease Indenture Estate from said Lien provided that the Indenture Trustee shall have first received a certificate in form and substance reasonably satisfactory to the Indenture Trustee, executed by the Lessee or the Owner Trustee, accompanied by an opinion of counsel reasonably satisfactory to the Indenture Trustee, each of which shall be to the effect that all necessary actions have been or are being taken simultaneously with such

release in connection with the proposed action to comply with the terms of this Indenture and the relevant Transaction Documents and that, in the case of releases required by Section 8(c) of the Facility Lease, all documents necessary to perfect, protect and preserve the lien created by this Indenture with respect to the Capital Improvements which are to be subjected to the lien of this Indenture have been duly authorized and properly executed and have been delivered to the Indenture Trustee, it being understood that insofar as such certificate and opinion relates to the due authority of, and proper execution of documents by, the Owner Trustee, the Lessee and the Indenture Trustee may rely upon a certificate of, and accompanying opinion of counsel to, the Owner Trustee. Notwithstanding the foregoing, (i) no opinion of counsel need be delivered with respect to the release by the Indenture Trustee of security with an aggregate value of less than \$500,000 unless specifically requested by the Indenture Trustee, provided such proposed action complies with the terms of the Facility Lease, and (ii) to the extent that the Lessee and the Owner Trustee shall mutually agree on, and shall deliver a certificate to the Indenture Trustee evidencing such agreement with respect to, a new arrangement relating to the Real Property Interest, the Indenture Trustee shall take all actions mutually requested by the Owner Trustee and the Lessee set forth in such certificate.

SECTION 2.4. Release of Lien on Lease Indenture Estate.

(a) Upon the Indenture Trustee's determination, evidenced by its certificate delivered to (1) during the period that any Initial Series Notes are Outstanding, the Agent, (2) during the period that Funding Corp is the Holder of the Notes, the Collateral Trust Trustee, or (3) at all other times, the Holders of the Outstanding Notes, that (i) it has received, or provision has been made in accordance with paragraph (c) of this Section 2.4 for, full payment of all principal of and premium, if any, and interest on the Notes and any other sums payable to the Indenture Trustee and the Holders of the Notes under this Indenture, the Notes and any of the Granting Clause Documents, and (ii) all Trustee's Expenses shall have been paid in full or provision satisfactory to the Indenture Trustee shall have been made for such payment,

(A) the lien and all other estate and rights granted by this Indenture shall cease, determine and terminate and all of the property, rights and interests included in the Lease Indenture Estate shall revert to and revest in the Owner Trustee without any other act or formality whatsoever, and

(B) the Indenture Trustee shall, at the request of the Owner Trustee, execute and deliver to the Owner Trustee such termination statements, releases or other instruments presented to the Indenture Trustee by or at the direction of the Owner Trustee as shall be requisite to evidence the satisfaction and discharge of this Indenture and the lien hereby created with respect to the Lease Indenture Estate, to release or reconvey to the Owner Trustee or as directed by the Owner Trustee all the Lease Indenture Estate, freed and discharged from the provisions herein contained with respect thereto, and to release the Owner Trustee from its covenants herein contained.

(b) Upon satisfaction of the conditions, and receipt by the Indenture Trustee of the Assumption Agreement and other documents and opinions, described in Section 3.9(b), the Indenture Trustee shall, at the request of the Owner Trustee, execute and deliver to the Owner Trustee such agreements, releases or other instruments presented to the Indenture Trustee by or at the direction of the Owner Trustee as shall be requisite to evidence the satisfaction and discharge of this Indenture as to the Owner Trustee and to release the Owner Trustee from its covenants herein contained. The satisfaction and discharge of this Indenture as to the Owner Trustee shall not operate as a satisfaction and discharge of the lien created hereby with respect to the Lease Indenture Estate notwithstanding the fact that the Facility Lease may have terminated as a matter of law and that, as a consequence, any rights of the Owner Trustee under the ANPP Participation Agreement and the Assignment and Assumption may no longer exist.

(c) Any Note, other than any of the Initial Series Notes, shall, prior to the maturity or redemption date thereof, be deemed to have been paid within the meaning and with the effect expressed in this Section 2.4(c) if (i) there shall have been deposited with the Indenture Trustee either moneys in an amount which shall be sufficient, or direct obligations of or obligations the principal of and interest on which are

unconditionally guaranteed by the United States of America or certificates of an ownership interest in the principal of or interest on obligations of or guaranteed as to principal and interest by the United States of America (Federal Securities), in each case which shall not contain provisions permitting the redemption thereof at the option of the issuer, the principal of and the interest on which when due, and without any reinvestment thereof, will provide moneys in an amount which shall be sufficient, together with the moneys, if any, deposited with or held by the Indenture Trustee at the same time (such sufficiency to be established by the delivery to the Indenture Trustee of a certificate of an independent public accountant), to pay when due the principal of and premium, if any, and interest due and to become due on said Note on and prior to the redemption date or maturity date thereof, as the case may be, and (ii) in the event said Note does not mature or is not to be redeemed within the next 45 days, the Indenture Trustee shall have been given irrevocable instructions to give, as soon as practicable, a notice to the registered Holder of such Note that the deposit required by subclause (i) above has been made with the Indenture Trustee and that said Note is deemed to have been paid in accordance with this Section 2.4(c) and stating such maturity or redemption date upon which moneys are to be available for the payment of the principal of and premium, if any, and interest on said Note. Neither the Federal Securities nor moneys deposited with the Indenture Trustee pursuant to this Section 2.4(c) or principal or interest payments on any such Federal Securities 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 on said Note; provided, however, that any cash received from such principal or interest payments on such Federal Securities deposited with the Indenture Trustee, shall be reinvested pursuant to Section 8.8 in Federal Securities. At such time as any Note shall be deemed paid as aforesaid, it shall no longer be secured by or entitled to the benefits of the Lease Indenture Estate or, except as provided in Section 2.4(d), of this Indenture.

(d) So long as any Note as to which this Indenture has been discharged remains unpaid, this Indenture shall continue in effect with respect to such Note solely with respect to rights of registration of transfer, exchange or replacement of such Note, rights to receive payment of the principal thereof and premium,

if any, and interest thereon in accordance with the terms of this Indenture from such deposited funds or the proceeds of or interest on such Federal Securities and the correlative rights and responsibilities of the Indenture Trustee; provided, however, that, following such discharge, no claim for payment of principal of or premium, if any, or interest on such Note shall be made against the Owner Trustee or the Lease Indenture Estate other than as provided in this Section; provided, further, that the Owner Trustee, following such discharge, shall be released from any further duties or obligations under this Indenture and, except as expressly provided therein, any other Transaction Document.

SECTION 2.5. Severance.

The parties hereto understand and agree and it is their express intention that Unit 2 (including the Undivided Interest), each Capital Improvement and each part thereof is or shall be severed, and shall be and remain severed, from the real estate constituting the PVNGS Site and even if physically attached thereto, shall retain the character of personal property, shall be treated as personal property with respect to the rights of all persons whomsoever, shall not be or become fixtures or otherwise part of the real estate constituting the PVNGS Site, and, by virtue of its nature as personal property, shall not be affected in any way by any instrument dealing with the real estate constituting the PVNGS Site.

SECTION 2.6. Power of Attorney.

Subject to the other terms of this Indenture, the Owner Trustee hereby appoints, effective whenever an Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee the Owner Trustee's attorney-in-fact, irrevocably, with full power of substitution, to collect, ask, require, demand, receive and give acquittance for any and all moneys and claims for moneys due and to become due to the Owner Trustee under or arising out of the Lease Indenture Estate, to endorse any checks or other instruments or orders in connection therewith, and to take any action (including the filing of financing statements or other documents) or institute any proceedings which the Indenture Trustee may deem to be necessary or appropriate to protect and preserve the interest of the Indenture Trustee in the Lease Indenture Estate.

ARTICLE III

ISSUE, EXECUTION, AUTHENTICATION, FORM AND REGISTRATION OF NOTES

SECTION 3.1. Limitation on Notes.

No Notes may be issued under the provisions of, or become secured by, this Indenture except in accordance with the provisions of this Article III. No Note shall be issued in an original principal amount of less than \$150,000.

SECTION 3.2. Execution of Notes.

All Notes shall be manually executed on behalf of the Owner Trustee by one of its Responsible Officers. In case any Responsible Officer of the Owner Trustee who shall have executed any of the Notes shall cease to be such a Responsible Officer before such Notes so executed shall have been authenticated by the Indenture Trustee and delivered or disposed of by the Owner Trustee, such Notes nevertheless may be authenticated and delivered or disposed of as though the person who executed such Notes had not ceased to be such a Responsible Officer of the Owner Trustee; and any Note may be executed on behalf of the Owner Trustee by such person as, at the actual time of execution of such Note, shall be a Responsible Officer of the Owner Trustee, although at the date of such Note any such person was not such a Responsible Officer.

SECTION 3.3. Effect of Certificate of Authentication.

Only such Notes as shall bear thereon a certificate of authentication substantially in the following form manually executed by the Indenture Trustee shall be entitled to the benefits of this Indenture or be valid or obligatory for any purpose. Such certificate of authentication of the Indenture Trustee upon any Note executed by the Owner Trustee shall be conclusive evidence that the Note so authenticated was duly issued, authenticated and delivered under this Indenture:

This Note is one of the series of Notes referred to therein and in the within-mentioned Indenture.

CHEMICAL BANK
as Indenture Trustee,

By _____
Authorized Officer

SECTION 3.4. Creation of the Initial Series Notes; Aggregate Principal Amount, Dating and Terms.

(a) There is hereby created and established a separate series of Notes of the Owner Trustee designated: "Nonrecourse Promissory Note, Initial Series", which shall be substantially in the form of, and shall contain the terms set forth in, Exhibit A hereto, and are herein referred to as the "Initial Series Notes".

(b) The Initial Series Notes shall be executed and issued by the Owner Trustee and authenticated and delivered by the Indenture Trustee on the date and to the Persons specified by the Owner Trustee in its request and authorization for issuance, shall be dated the date specified by the Owner Trustee in its request and authorization for issuance, and shall be in the form of registered Notes registered in the names of the Persons designated in the Owner Trustee's request and authorization for issuance or its registered assigns.

(c) The Initial Series Notes shall bear interest on the principal amount thereof from time to time Outstanding from the date thereof until paid at the rates of interest set forth in the form of the Initial Series Notes. The principal amount of the Initial Series Notes shall be payable as set forth in the Schedule of Principal Payments attached thereto. Interest on the Initial Series Notes shall be due and payable at the times specified in the form of Initial Series Notes.

SECTION 3.5. Additional Notes.

(1) Subject to Section 3.6, and upon condition that (A) no Default or Event of Default or Indenture Event of Default has occurred and is continuing and (B) payments pursuant to the Facility Lease of Basic Rent, Casualty Value, Special Casualty Value and of amounts in respect of the Cure Option are sufficient to pay as and when due all amounts of principal of and premium, if any, and interest on all Outstanding Notes, after taking into account the issuance of such Additional Notes and any related redemption, Additional Notes of the Owner Trustee may be issued under and secured by this Indenture, at any time or from time to time, in addition to the Initial Series Notes and subject to the conditions hereinafter provided in this Section, for cash in the amount of the original principal amount of such Additional Notes, but only for the purpose of (i) refunding any previously issued series of Notes, in whole or in part and/or (ii) providing funds for the payment of all or any portion of the Supplemental Financing Amount relating to Capital Improvements made or installed from time to time pursuant to the Facility Lease and/or (iii) providing funds to be paid to the Owner Trustee in the event of a partial return of the Investment to the Owner Trustee as contemplated by Section 2(d) or 2(e) of the Participation Agreement; provided, however, that (x) in the case of Notes issued for the purposes set forth in clause (ii) or (iii) of this Section 3.5, no Note shall be issued by the Owner Trustee pursuant to this Section 3.5 unless such Notes may be pledged in accordance with the Collateral Trust Indenture and serve as the basis for Additional Bonds and (y) in the case of Notes issued for the purposes set forth in clause (i) or (iii) of this Section 3.5, no Note shall be issued by the Owner Trustee pursuant to this Section 3.5 unless Section 2(d) and/or 2(e) of the Participation Agreement (if applicable) shall have been complied with and provided, further that so long as any Initial Series Notes are Outstanding, Additional Notes may be issued only if all principal of, and premium, if any, and accrued interest on, all such Initial Series Notes are simultaneously paid in full.

(2) Before any Additional Notes shall be issued under the provisions of this Section 3.5, the Owner Trustee shall have received from the Equity Participant, and delivered to the Indenture Trustee not less than 10 nor more than 30 days prior to the proposed

date of issuance of such Additional Notes as set forth in the below-mentioned request and authorization, a request and authorization to issue Additional Notes, which request and authorization shall include the amount of such Additional Notes, the date of issuance of such Additional Notes and details with respect thereto which are not inconsistent with this Section. Additional Notes shall have a designation so as to distinguish each Series of Additional Notes from each other series of Additional Notes but otherwise each such series shall be substantially similar in terms to each other such series, shall specify maturity dates, rank *pari passu* with all Notes then Outstanding, be dated their respective dates of authentication, bear interest at such rates (which may be fixed or floating) as shall be indicated in the aforementioned request and authorization, and shall be stated to be payable by their terms not later than the last day of the Basic Lease Term.

(3) Except as to any differences in the maturity dates and amortization schedules of the Additional Notes or the rate or rates of interest thereon and the date or dates such interest is payable or the provisions for redemption with respect thereto, if any, such Additional Notes shall be on a parity with, and shall be entitled to the same benefits and security of this Indenture as, other Notes issued pursuant to the terms hereof.

(4) The terms, conditions and designations of such Additional Notes (which shall be consistent with this Indenture) shall be set forth in an indenture supplemental to this Indenture executed by the Owner Trustee and the Indenture Trustee. Such Additional Notes shall be executed as provided in Section 3.2 and deposited with the Indenture Trustee for authentication, but before such Additional Notes shall be authenticated and delivered by the Indenture Trustee there shall be filed with the Indenture Trustee, in addition to the other documents and certificates required by this Section 3.5, the following, all of which shall be dated as of the date of the supplemental indenture:

(a) a copy of such supplemental indenture (which shall include the form of such series of Notes in respect thereof);

(b) a certificate of a Responsible Officer of the Owner Trustee (i) stating that to the best of his knowledge, no Default or Event of Default or Indenture

Event of Default has occurred and is continuing, (ii) stating that the conditions in respect of the issuance of such Additional Notes contained in this Section 3.5 have been satisfied, (iii) specifying the amount of the costs and expenses relating to the issuance and sale of such Additional Notes, (iv) stating that payments pursuant to the Facility Lease of Basic Rent, Casualty Value and Special Casualty Value and of amounts in respect of the exercise of the Cure Option are sufficient to pay as and when due all amounts of principal of and premium, if any, and interest on all the Outstanding Notes, after taking into account the issuance of such Additional Notes and any related redemption, and (v) in the case of Notes issued for the purpose set forth in clause (ii) of Section 3.5(1), stating that, to the best of his knowledge, all conditions to the related Supplemental Financing as set forth in Section 8(f) of the Facility Lease have been satisfied or waived in accordance with such Section 8(f);

(c) such additional documents, certificates and opinions as shall be reasonably requested by, and acceptable to, the Owner Trustee and the Indenture Trustee;

(d) a request and authorization to the Indenture Trustee by or on behalf of the Owner Trustee to authenticate and deliver such Additional Notes to or upon the order of the Person or Persons noted in such request at the address set forth therein, and in such principal amounts as are stated therein, upon payment to the Indenture Trustee, but for the account of the Owner Trustee, of the sum or sums specified in such request and authorization; and

(e) an opinion of counsel to the effect that the conditions precedent required under this Indenture for the issuance of such Additional Notes have been complied with.

When the documents referred to in the foregoing clauses (a) through (e) above shall have been filed with the Indenture Trustee and when the Additional Notes described in the above-mentioned request and authorization shall have been executed and authenticated as required by this Indenture, the Indenture Trustee shall deliver such Additional Notes in the manner described in clause (d) above, but only upon payment to the Indenture Trustee of the sum or sums specified in such request and authorization.

SECTION 3.6. Security for and Parity of Notes.

All Notes issued and Outstanding hereunder shall rank on a parity with each other and shall as to each other be secured equally and ratably by this Indenture, without preference, priority or distinction of any thereof over any other by reason of difference in time of issuance or otherwise.

SECTION 3.7. Source of Payments Limited.

All payments to be made by the Owner Trustee under this Indenture or on the Notes shall be made only from the Lease Indenture Estate and the Trust Estate. Each Holder of a Note, by its acceptance of such Note, and the Indenture Trustee agree that they will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to such Holder or the Indenture Trustee as herein provided and that neither the Equity Participant nor, except as expressly provided in this Indenture, the Owner Trustee nor the Indenture Trustee, shall be personally liable to such Holder of a Note or the Indenture Trustee, as the case may be, for any amounts payable hereunder or under such Note; provided, however, that in the event, and to the extent, that the Lessee shall assume all the obligations and liabilities of the Owner Trustee hereunder and under the Notes pursuant to Section 3.9(b), then all payments to be made under this Indenture and the Notes shall be made only from payments made by the Lessee under the Notes in accordance with the Assumption Agreement referred to in Section 3.9(b) and, subject to Section 2.4 hereof, from the Lease Indenture Estate and each Holder of a Note and the Indenture Trustee agree that in such event they will look solely to the Lessee and the Lease Indenture Estate for such payment. Nothing herein contained shall be interpreted as affecting the duties and obligations of the Indenture Trustee set forth in Section 7.4.

In furtherance of the foregoing, to the fullest extent permitted by law, each Holder of a Note (and each assignee of such Person), by its acceptance thereof, and the Indenture Trustee agree, as a condition to the Notes being secured under this Indenture, that neither such Holder nor the Indenture Trustee will exercise any statutory right to negate the agreements set forth in this Section 3.7.

SECTION 3.8. Place and Medium of Payment.

The principal of and premium, if any, and interest on each Note shall be payable at the Indenture Trustee's Office in immediately available funds 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. Notwithstanding the foregoing or any provision in any Note to the contrary, if so requested by the Holder of any Note, by written notice to the Indenture Trustee, all amounts (other than the final payment) payable with respect to such obligation shall be paid by crediting the amount to be distributed to such Holder to an account maintained by such Holder with the Indenture Trustee or by the Indenture Trustee's transferring such amount by wire, with such wire transfer to be initiated by such time as to permit, to the extent practicable, oral confirmation thereof (specifying the wire number) to be given no later than 1:00 P.M. New York City time on the date scheduled for payment, but only to the extent of funds available for such wire transfer, to such other bank in the United States having wire transfer facilities, including a Federal Reserve Bank, as shall have been specified in such notice, for credit to the account of such Holder maintained at such bank, any such credit or transfer pursuant to this Section 3.8 to be in immediately available funds, without any presentment or surrender of such Note. Final payment of any such Note shall be made only against surrender of such Note at the Indenture Trustee's Office.

SECTION 3.9. Prepayment of Notes; Assumption by Lessee; Notice of Assumption or Prepayment.

(a) Notes shall be subject to prepayment (other than through application of the installment payments on such Notes) from time to time only as provided in this Indenture and as otherwise specifically provided, with respect to Notes of a particular series, in such Notes.

(b) In the event of the occurrence of a Deemed Loss Event or Event of Loss or exercise of the Cure Option, and upon receipt by the Indenture Trustee of the documents listed below, (i) all the obligations and liabilities of the Owner Trustee hereunder and under the Notes shall be assumed by the Lessee, (ii) if any Initial Series Notes are Outstanding, the Lessee shall assume all obligations and liabilities of the Owner

Trustee thereunder pursuant to agreements substantially in the form of, and containing the terms set forth in, Exhibit C hereto (such Initial Series Notes when assumed pursuant to such agreements are herein referred to as the Bank Exchange Notes), and (iii) the Owner Trustee shall be released and discharged without further act or formality whatsoever from all obligations and liabilities hereunder and under the Notes:

(1) a duly executed Assumption Agreement substantially in the form of Exhibit B hereto;

(2) an opinion of counsel, addressed to the Indenture Trustee and the Holders of the Outstanding Notes, to the effect that the conditions precedent required by this Indenture for such assumption have been complied with, that the Assumption Agreement has been duly authorized, executed and delivered on behalf of the Lessee, that no Governmental Action is necessary or required in connection therewith (or if any such Governmental Action is necessary or required, that the same has been duly obtained and is in full force and effect), and that the Assumption Agreement is a legal, valid and binding agreement and obligation of the Lessee, enforceable in accordance with its terms (except as limited by bankruptcy, insolvency or similar laws of general application affecting the enforcement of creditors' rights generally and equitable principles);

(3) copies of all Governmental Actions referred to in such opinion;

(4) an indenture supplemental to this Indenture which shall, among other things, confirm the release of the Owner Trustee thereby effected and may contain provisions appropriately amending references to the Facility Lease in this Indenture;

(5) a certificate of a Responsible Officer of the Lessee stating that (i) the conditions precedent required by this Indenture for such assumption have been complied with, (ii) such assumption is permitted by the provisions of the Lessee's Restated Articles of Incorporation and By-Laws and has been authorized by all requisite corporate action, and (iii) the Lessee is not insolvent within the meaning of any applicable preferential

transfer, fraudulent conveyance or bankruptcy law; and

(6) if Initial Series Notes are to be exchanged for Bank Exchange Notes, at the request of the Holders of the Initial Series Notes, an Assignment, Assumption and Further Agreement between the Lessee and the Indenture Trustee substantially in the form of the Assignment and Assumption, with such changes, if any, as the Indenture Trustee shall reasonably request to enable the Holders of the Notes to benefit from their security interest in the Lease Indenture Estate..

(c) Notice of any assumption or prepayment of Notes shall be given to the registered Holders of the Notes which have been assumed or are to be prepaid (and any assignee of a registered Holder which has given the Indenture Trustee written notice of such assignment) as promptly as practicable after the Indenture Trustee is notified thereof, and, in the case of prepayment, in no event less than 30 days before the date fixed for prepayment (provided the Indenture Trustee receives such notification at least three Business Days before such 30th day), in the event of the exercise by the Lessee or the Owner Trustee, as the case may be, of its option to terminate the Facility Lease pursuant to Section 14 thereof or in the event of the exercise by the Lessee of the Cure Option.

SECTION 3.10. Mutilated, Destroyed, Lost or Stolen Notes.

If any Note shall become mutilated or shall be destroyed, lost or stolen, the Owner Trustee shall, upon the written request of the Holder of such Note, execute, and the Indenture Trustee shall authenticate and deliver in replacement thereof, a new Note, payable in the same original principal amount and dated the same date and of the same series as the Note so mutilated, destroyed, lost or stolen. The Indenture Trustee shall make a notation on each new Note of the amount of all payments of principal theretofore made on the Note so mutilated, destroyed, lost or stolen and the date to which interest on such old Note has been paid. If the Note being replaced has been mutilated, such Note shall be delivered to the Indenture Trustee who shall then deliver a certificate of destruction of the type required by Section 4.3. If the Note being replaced has been destroyed, lost or stolen, the Holder of such Note shall furnish to the Lessee, the Owner Trustee and the

Indenture Trustee a bond or surety agreement of such Holder as shall be satisfactory to them to save the Lessee, the Owner Trustee, the Indenture Trustee, the Trust Estate and the Lease Indenture Estate harmless from any loss, however remote, including claims for principal of, and premium, if any, and interest on the purportedly destroyed, lost or stolen Note, together with evidence satisfactory to the Lessee, the Owner Trustee and the Indenture Trustee of the destruction, loss or theft of such Note and of the ownership thereof; provided, however, that if the Holder of such Note is the Collateral Trust Trustee, the unsecured written undertaking of the Collateral Trust Trustee, in its individual capacity, shall be sufficient indemnity for purposes of this Section.

SECTION 3.11. Allocation of Principal and Interest.

In the case of each Note, each payment of principal thereof and interest thereon shall be applied, first, to the payment of accrued but unpaid interest on such Note (as well as any interest on overdue principal or, to the extent permitted by law, interest) to the date of such payment, second, to the payment of the principal amount of, and premium, if any, on such Note then due (including any overdue installment of principal) thereunder and third, the balance, if any, remaining thereafter, to the balance of the payment of the principal amount of, and premium, if any, on such Note.

SECTION 3.12. Certain Adjustments to Amortization Schedules of Notes.

The schedules of principal amortization attached to the Outstanding Refunding Notes may be adjusted at the discretion of the Owner Trustee at one time prior to June 30, 1989; provided, however, such adjustment only may be made in connection with an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease. If the Owner Trustee shall elect to make the foregoing adjustment, the Owner Trustee shall deliver to the Indenture Trustee and to the Lessee at least 60 days prior to the first payment date (specified on the schedules hereto) proposed to be affected by such adjustment, a certificate of the Owner Trustee (x) stating that the Owner Trustee has elected to make such adjustment, (y) setting forth the revised schedules of principal amortization for each of the Outstanding Refunding Notes and (z) attaching calculations showing that the average life of the Outstanding Refunding Notes

will not be reduced or increased except as permitted by this Section 3.12. The Indenture Trustee may rely on such Owner Trustee certificate and shall have no duty with respect to the calculations referred to in the foregoing clause (2).

ARTICLE IV

REGISTRATION, TRANSFER, EXCHANGE, CANCELLATION AND OWNERSHIP OF NOTES

SECTION 4.1. Register of Notes.

The Indenture Trustee on behalf of the Owner Trustee shall maintain at the Indenture Trustee's Office a register for the purpose of registration, and registration of transfer and exchange, of the Notes by series and in which shall be entered the names and addresses of the owners of such Notes and the principal amounts of the Notes owned by them, respectively. For these purposes, the Indenture Trustee is hereby appointed transfer agent and registrar for the Notes.

SECTION 4.2. Registration of Transfer or Exchange of Notes.

A Holder of a Note intending to register the transfer of any Outstanding Note held by such Holder (including any transfer in the form of a pledge or assignment) or to exchange any Outstanding Note held by such Holder for a new Note or Notes of the same series may surrender such Outstanding Note at the Indenture Trustee's Office, together with the written request of such Holder, or of its attorney duly authorized in writing, in each case with signatures guaranteed, for the registration of such Note in the name of any pledgee or assignee (in the case of a transfer in the form of a pledge or assignment) or for the issuance of a new Note or Notes of the same series, specifying the authorized denomination or denominations of any new Note or Notes to be issued and the name and address of the Person or Persons in whose name or names the Note or Notes are to be registered (either as pledgee or assignee or as owner). Promptly upon receipt by the Indenture Trustee of the foregoing and satisfaction of the requirements of Sections 4.5 and 4.6, the Indenture Trustee shall

register such Note or Notes in the name or names of the Person or Persons as shall be specified in the written request and, in the case in which a new Note or Notes are to be issued, the Owner Trustee shall execute and the Indenture Trustee shall authenticate and deliver such new Note or Notes of the same series, in the same aggregate principal amount and dated the same date as the Outstanding Note surrendered, in such authorized denomination or denominations as shall be specified in the written request. The Indenture Trustee shall make a notation on each new Note of the amount of all payments of principal theretofore made on the old Note or Notes in exchange or transfer for which any new Note has been issued and the date to which interest on such old Note or Notes has been paid.

SECTION 4.3. Cancellation of Notes.

All Notes surrendered to the Indenture Trustee for payment in full, prepayment in full or registration of transfer or exchange shall be cancelled by it; and no Notes shall be issued in lieu thereof except as expressly permitted by this Indenture. The Indenture Trustee shall destroy cancelled Notes held by it in a manner satisfactory to the Owner Trustee and deliver a certificate of destruction to the Owner Trustee. If the Owner Trustee shall acquire any of the Notes, such acquisition shall not operate as a redemption of or the satisfaction of the indebtedness represented by such Notes unless and until the same shall be delivered to the Indenture Trustee for cancellation.

SECTION 4.4. Limitation on Timing of Registration of Notes.

The Indenture Trustee shall not be required to register transfers or exchanges of Notes on any date fixed for the payment or prepayment of principal of or interest on the Notes or during the fifteen days preceding any such date.

SECTION 4.5. Restrictions on Transfer Resulting from Federal Securities Laws; Legend.

If not prohibited by the Securities Act, each Note shall be delivered to the initial Holder thereof without registration of such Note under the Securities Act and without qualification of this Indenture under the Trust Indenture Act. Prior to any transfer of any Note, in whole or in part, to any Person other than the

Collateral Trust Trustee, the Holder thereof shall furnish to the Lessee, the Indenture Trustee and the Owner Trustee an opinion of counsel, which opinion and which counsel shall be reasonably satisfactory to the Indenture Trustee, the Owner Trustee and the Lessee, to the effect that such transfer will not violate the registration provisions of the Securities Act or require qualification of this Indenture under the Trust Indenture Act, and all Notes issued hereunder shall be endorsed with a legend which shall read substantially as follows:

This Note has not been registered under the Securities Act of 1933 and may not be transferred, sold or offered for sale in violation of such Act.

SECTION 4.6. Charges upon Transfer or Exchange of Notes.

As a further condition to registration of transfer or exchange of any Note, the Indenture Trustee and the Owner Trustee may charge the Holder thereof for any stamp taxes or governmental charges required to be paid with respect to such registration of transfer or exchange.

SECTION 4.7. Inspection of Register of Notes.

The register of the Holders of the Notes referred to in Section 4.1 shall at all reasonable times be open for inspection by any Holder of a Note. Upon request by any Holder of a Note, or the Owner Trustee or the Lessee, the Indenture Trustee shall furnish such Person, at the expense of such Person, with a list of the names and addresses of all Holders of Notes entered on the register kept by the Indenture Trustee indicating the series, principal amount and number of each Note held by each such Holder.

SECTION 4.8. Ownership of Notes.

(a) Prior to due presentment for registration of transfer of any Note, the Owner Trustee and the Indenture Trustee may deem and treat the Holder of record of such Note as the absolute owner of such Note for the purpose of receiving payment of all amounts payable with respect to such Note and for all other purposes, and neither the Owner Trustee nor the

Indenture Trustee shall be affected by any notice to the contrary.

(b) The Owner Trustee and the Indenture Trustee may, in their discretion, treat the Holder of record of any Note as the owner thereof without actual production of such Note for any purpose hereunder, except as provided in the last sentence of Section 3.8.

(c) Neither the Owner Trustee nor the Indenture Trustee shall be bound to take notice of or carry out the execution of any trust in respect of any Note, and may register the transfer of the same on the direction of the Holder of record thereof, whether named as trustee or otherwise, as though such Holder were the beneficial owner thereof.

(d) The receipt by the Holder of record of any Note of any payment of principal, premium or interest shall be a good discharge to the Owner Trustee and the Indenture Trustee for the same and neither the Owner Trustee nor the Indenture Trustee shall be bound to inquire into the title of any such Holder.

ARTICLE V

RECEIPT, DISTRIBUTION AND APPLICATION OF INCOME AND PROCEEDS FROM THE LEASE INDENTURE ESTATE

SECTION 5.1. Basic Rent and Interest on Overdue Installments of Basic Rent.

Except as otherwise provided in Section 5.3 or 5.7, each payment of Basic Rent, as well as any payment of Supplemental Rent representing interest on overdue installments of Basic Rent, received by the Indenture Trustee at any time, shall be distributed by the Indenture Trustee in the following order of priority: first, so much of such payment as shall be required to pay in full the aggregate amount of the payment or payments of principal and premium, if any, and/or interest (as well as any interest on overdue principal or, to the extent permitted by law, interest) then due and unpaid on all Notes shall be distributed to the Holders of the Notes ratably, without priority of one over the other, in the proportion that the aggregate amount of such

payment or payments then due and unpaid on all Notes held by each such Holder on such date bears to the aggregate amount of such payment or payments then due and unpaid on all Notes Outstanding on such date, without priority of interest over principal or principal over interest; and second, the balance, if any, of such payment remaining thereafter shall be distributed, concurrently with any distribution pursuant to clause first hereof, to the Owner Trustee or as the Owner Trustee may direct. If there shall not otherwise have been distributed on any date (or within any applicable period of grace), pursuant to this Section 5.1, the full amount then distributable pursuant to clause first of this Section 5.1, the Indenture Trustee shall distribute other payments of the character referred to in Sections 5.4 and 5.5 then held by it or thereafter received by it, except as otherwise provided in Section 5.3, to the Holders of all Notes to the extent necessary to enable it to make all the distributions then due pursuant to such clause first; provided that to the extent any distribution is made from amounts held pursuant to Section 5.4 and the Lessee subsequently makes the payment of Basic Rent or Supplemental Rent in respect of which such distribution was made, such payment of Basic Rent or Supplemental Rent shall, unless a Default or an Event of Default shall have occurred and be continuing, be applied to the purpose for which such amount held pursuant to Section 5.4 had been held, subject, in all cases, to the terms of Section 5.4. The portion of each such payment made to the Indenture Trustee which is to be distributed by the Indenture Trustee in payment of Notes shall be applied in accordance with Section 3.11. Any payment received by the Indenture Trustee pursuant to Section 6.8 shall be distributed to the Holders of the Notes, ratably, without priority of one over the other, in the proportion that the amount of such payment or payments then due and unpaid on all Notes held by each such Holder bears to the aggregate amount of the payments then due and unpaid on all Notes Outstanding. Amounts distributed by the Indenture Trustee pursuant to this Section 5.1 shall be distributed as promptly as practicable after such amounts are actually received by the Indenture Trustee; in the event the Indenture Trustee shall be directed to make payments to the Holder of any Note by wire transfer in accordance with Section 3.8, any amounts received by the Indenture Trustee after 1:00 P.M., New York City time, may be so distributed on the following Business Day.

SECTION 5.2. Amounts Received as Result of Event of Loss, Deemed Loss Event, Exercise of Option to Terminate or Exercise of Cure Option.

If an Event of Loss or Deemed Loss Event shall occur or the Lessee shall exercise the Cure Option, any amounts of Casualty Value, Special Casualty Value or Fair Market Sales Value received or held by the Indenture Trustee in respect of such Event of Loss or Deemed Loss Event or exercise of the Cure Option shall, except as otherwise provided in Section 5.3 be distributed forthwith to the Equity Participant. If the Lessee or Owner Trustee, as the case may be, shall exercise its option to terminate the Facility Lease pursuant to Section 14 thereof, then there shall be prepaid, on the date payments or proceeds with respect thereto are received by the Indenture Trustee (or as soon thereafter as practicable) under Section 14 of the Facility Lease, the unpaid principal amount of all Notes, together with the premium, if any, and all accrued but unpaid interest thereon to the date of such prepayment. Notice of such prepayment shall be given as provided in Section 3.9(c) and may provide that it is subject to receipt of funds for such prepayment. Except as otherwise provided in Section 5.3 or 5.7, any payments received and amounts realized by the Indenture Trustee upon exercise of the Lessee's or the Owner Trustee's option to terminate the Facility Lease under Section 14 thereof shall in each case be distributed on the date of prepayment as provided in clauses first, second and fifth of Section 5.3.

SECTION 5.3. Amounts Received After, or Held at Time of, Indenture Event of Default under Section 6.2.

Except as otherwise provided in Section 5.7, all payments received and amounts realized by the Indenture Trustee in respect of the Lease Indenture Estate (including any amounts realized by the Indenture Trustee from the exercise of any remedies pursuant to the Facility Lease or Article VI of this Indenture) after an Indenture Event of Default referred to in Section 6.2 shall have occurred and be continuing and the Notes have been accelerated pursuant to Section 7.1, as well as all payments thereafter received or amounts then held by the Indenture Trustee as part of the Lease Indenture Estate, shall be distributed by the Indenture Trustee in the following order of priority:

first, so much of such payments or amounts as shall be required to reimburse the Indenture Trustee for any Trustee's Expenses (to the extent not previously reimbursed) and to pay the reasonable remuneration of the Indenture Trustee, shall be applied by the Indenture Trustee to such reimbursement and payment;

second, so much of such payments or amounts remaining as shall be required to pay in full the aggregate unpaid principal amount of all Notes, together with premium, if any, plus accrued but unpaid interest (as well as interest on overdue principal and, to the extent permitted by law, on overdue interest and any other amounts owing thereunder) thereon to the date of distribution, shall be distributed to the Holders of such Notes and in case the aggregate amount so to be distributed shall be insufficient to pay all such Notes in full as aforesaid, then ratably, without priority of one over the other, in the proportion that the aggregate unpaid principal amount of all such Notes held by each such Holder, together with premium, if any, plus accrued but unpaid interest thereon to the date of distribution bears to the aggregate unpaid principal amount of all Notes, together with premium, if any, plus accrued but unpaid interest thereon to the date of distribution;

third, so much of such payments or amounts remaining as shall be required to pay the present or former Holders of the Notes the amounts payable to them as Indemnitées (to the extent not previously reimbursed) shall be distributed to such Holders; and in case the aggregate amount so to be paid to all such Holders in accordance with this clause third shall be insufficient to pay all such amounts as aforesaid, then ratably, without priority of one over the other, in the proportion that the amount of such indemnity or other payments to which such Person is entitled bears to the aggregate amount of such indemnity or other payments to which all such Persons are entitled;

fourth, the balance, if any, of such payments or amounts remaining shall be applied to the payment of any other indebtedness at the time due and owing to the Indenture Trustee or the Holders of the Notes which this Indenture by its terms secures; and

fifth, the balance, if any, of such payments or amounts remaining thereafter shall be distributed to or upon the direction of the Owner Trustee.

SECTION 5.4. Amounts Received for Which Provision Is Made in a Transaction Document.

Except as otherwise provided in Section 5.1, 5.2, 5.3 or 5.7, any payments received by the Indenture Trustee in respect of the Lease Indenture Estate for which provision as to the application thereof is made in a Transaction Document shall be applied to the purpose for which such payment was made in accordance with the terms of such Transaction Document, as determined from instructions or other information accompanying such payment.

SECTION 5.5. Amounts Received for Which No Provision Is Made.

Except as otherwise provided in Section 5.1, 5.2, 5.3 or 5.7, any payments received and any amounts realized by the Indenture Trustee in respect of the Lease Indenture Estate (a) for which no provision as to the application thereof is made in a Transaction Document or elsewhere in this Article V shall be held by the Indenture Trustee as part of the Lease Indenture Estate, and (b) to the extent received or realized at any time after payment in full of the principal of and premium, if any, and interest on all the Notes, as well as any other amounts remaining as part of the Lease Indenture Estate after payment in full of the principal of and premium, if any, and interest on all the Notes, shall be distributed by the Indenture Trustee in the order of priority set forth in Section 5.3 (omitting clause second thereof).

SECTION 5.6. Payments to Owner Trustee.

Unless otherwise directed by the Owner Trustee, all payments to be made to the Owner Trustee hereunder shall be made to the Equity Participant by wire transfer of immediately available funds as soon as practicable but in any event no later than the close of business on the date of receipt (assuming the Indenture Trustee has received such funds prior to 3:00 P.M., New York City time, on the same day) to such account at such bank or trust company as the Equity Participant shall from time to time designate in writing to the Indenture Trustee.

SECTION 5.7. Excepted Payments.

Anything in this Article V or elsewhere in this Indenture to the contrary notwithstanding, any Excepted Payment received at any time by the Indenture Trustee shall be distributed as promptly as practicable to the Person entitled to receive such Payment.

ARTICLE VI

REPRESENTATIONS, WARRANTIES AND COVENANTS OF OWNER TRUSTEE; EVENTS OF DEFAULT; REMEDIES OF THE INDENTURE TRUSTEE

SECTION 6.1. Representations, Warranties and Covenants of Owner Trustee.

The Owner Trustee hereby covenants and agrees that (i) it will duly and punctually pay the principal of, and premium, if any, and interest on, the Notes in accordance with the terms thereof and this Indenture, (ii) it will not create or permit to exist and will promptly discharge any Lessor's Liens, (iii) so long as this Indenture shall remain in effect, it will not purchase or agree to purchase any property or asset other than the Undivided Interest and the Real Property Interest and other than as contemplated by the Transaction Documents, (iv) it will not, except with the prior written concurrence of the Indenture Trustee or as expressly provided in or permitted by this Indenture or with respect to the Trust Agreement or any property not constituting part of the Lease Indenture Estate, take any action which would result in an impairment of any Note or the obligation of the Lessee to pay any amount under the Facility Lease which is part of the Lease Indenture Estate (not in any event including in respect of Excepted Payments and Excepted Rights) or any of the other rights or security created or effected thereby, except as contemplated by the Transaction Documents, or (v) it will not issue, or incur any obligation in respect of, indebtedness for borrowed money except for its obligations in respect of Notes.

A signed copy of any amendment or supplement to the Trust Agreement shall be delivered by the Owner Trustee to the Indenture Trustee and the Lessee. This

Indenture and the Lease Indenture Estate shall not be affected by any action taken under or in respect of the Trust Agreement except as otherwise provided in or permitted by this Indenture. The Trust Agreement may not in any event be terminated by the Equity Participant or the Owner Trustee or revoked by the Equity Participant so long as any of the Notes remain Outstanding or the lien of this Indenture has not been released. The Owner Trustee may resign as Owner Trustee, appoint a successor Owner Trustee and take all necessary and proper action to constitute one or more Persons as co-trustee(s) jointly with the Owner Trustee or as separate trustee(s), all in accordance with the terms and conditions of Article IX of the Trust Agreement.

SECTION 6.2. Indenture Events of Default.

The term Indenture Event of Default, wherever used herein, shall mean any of the following events (whatever the reason for such Indenture Event of Default and whether it shall be voluntary or involuntary or come about or be effected by operation of law or pursuant to or in compliance with any judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

(a) any of the Events of Default specified in the following clauses of Section 15 of the Facility Lease: (1) clause (i)(y), except a failure of the Lessee to pay any amount which shall constitute an Excepted Payment; (2) clause (i)(x), except a failure of the Lessee to pay any amount which shall constitute an Excepted Payment or except where the Owner Trustee shall not have rescinded or terminated the Facility Lease pursuant to Section 16(a)(i) of the Facility Lease; or (3) clause (vii) or (x); or

(b) the rescission or termination of, or the taking of action by the Owner Trustee or the Equity Participant the effect of which would be to rescind or terminate, the Facility Lease, whether pursuant to Section 16(a)(i) of the Facility Lease or otherwise; or

(c) the exercise by the Owner Trustee or the Equity Participant of any of the remedies under Section 16(a)(v) of the Facility Lease prior to the happening of any of the events set forth in clause (b) of this Section 6.2; or

(d) any assignment, sublease or transfer by the Lessee in violation of Section 11(a) of the Facility Lease; or

(e) any failure by the Lessee to perform and observe Section 10(b)(3)(ii) or the first sentence of Section 10(b)(3)(i) of the Participation Agreement; or

(f) the Owner Trustee shall fail to make any payment in respect of the principal of, or premium, if any, or interest on, the Notes within five Business Days after the same shall have become due (other than by virtue of any failure by the Lessee to make any payment of Rent therefor); or

(g) the Owner Trustee shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 6.1 (other than clause (i) thereof), or the Equity Participant shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 7(b)(i) of the Participation Agreement, and, in any such case, such failure shall continue for a period of 30 days after notice thereof shall have been given to the Owner Trustee and the Equity Participant and the Lessee by the Indenture Trustee, specifying such failure and requiring it to be remedied; or

(h) any representation or warranty made by the Owner Trustee in Section 8(a) of the Participation Agreement, or any representation or warranty made by the Equity Participant in Section 7(a)(5) or (7) of the Participation Agreement, shall prove to have been incorrect in any material respect when such representation or warranty was made or given and remains material at the time of discovery thereof and, in any such case, the circumstances rendering such representation or warranty incorrect shall continue unremedied for a period of 30 days after notice thereof shall have been given to the Owner Trustee, the Equity Participant and the Lessee by the Indenture Trustee, specifying such circumstances and requiring them to be remedied, and the circumstances rendering such representation or warranty incorrect shall materially adversely affect the Holders of the Notes; or

(i) the Trust shall file any petition for dissolution or liquidation of the Trust or shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in

effect, or the Trust shall have consented to the entry of an order for relief in an involuntary case under any such law, or a receiver, custodian or trustee (or other similar official) shall be appointed for the Trust or shall take possession of any substantial part of its property (other than at the instance of the Indenture Trustee or the Noteholders), or the Trust shall make a general assignment for the benefit of its creditors, or shall enter into an agreement of composition with its creditors; or there shall be filed (other than at the instance of the Indenture Trustee or the Noteholders) against the Trust an involuntary petition in bankruptcy which results in an order for relief being entered or, notwithstanding that an order for relief has not been entered, the petition is not dismissed within 60 days of the date of the filing of the petition, or there shall be filed (other than at the instance of the Indenture Trustee or the Noteholders) under any Federal or state law relating to bankruptcy, insolvency or relief of debtors of any petition against the Trust for reorganization, composition, extension or arrangement with creditors which either (i) results in a finding or adjudication of insolvency of the Trust or (ii) is not dismissed within 60 days of the date of the filing of such petition; or

(j) the Equity Participant shall file any petition for dissolution or liquidation of the Equity Participant or shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or the Equity Participant shall have consented to the entry of an order for relief in an involuntary case under any such law, or shall fail generally to pay its debts as such debts become due (within the meaning of the Bankruptcy Code, or a receiver, custodian or trustee (or other similar official) shall be appointed for the Equity Participant or shall take possession of any substantial part of its property, or the Equity Participant shall make a general assignment for the benefit of its creditors, or shall enter into an agreement of composition with its creditors; or there shall be filed against the Equity Participant an involuntary petition in bankruptcy which results in an order for relief being entered or, notwithstanding that an order for relief has not been entered, the petition is not dismissed within 60 days of the date of the filing of the petition, or there shall be filed under any Federal or state law relating to bankruptcy, insolvency or relief of debtors of any petition against the Equity Participant for reorganization, composition,

extension or arrangement with creditors which either (i) results in a finding or adjudication of insolvency of the Equity Participant or (ii) is not dismissed within 60 days of the filing of such petition and any such event materially adversely affects the Holders of the Notes; or

(k) after a Special Transfer has been effected and amounts payable to the Equity Participant in connection therewith have been paid in full in accordance with Section 7(b)(4) of the Participation Agreement, any violation or breach of a warranty or covenant of the Lessee contained in the last paragraph of such Section 7(b)(4).

SECTION 6.3. Enforcement of Remedies.

(a) In the event that an Indenture Event of Default shall have occurred and be continuing, then and in every such case the Indenture Trustee, subject to paragraph (b) of this Section 6.3, may, and when required pursuant to the provisions of Article VII hereof shall, exercise any or all of the rights and powers and pursue, subject to any rights of the Lessee under the Facility Lease, (x) in the event such Indenture Event of Default (i) shall occur or be continuing after the effectiveness of a Special Transfer or assumption pursuant to Section 3.9(b) or (ii) is referred to in paragraph (f), (g), (h), (i), (j) or (k) of Section 6.2, any or all of the remedies then available pursuant to this Article VI and Article VII, or (y) subject to Section 6.11, in the event such Indenture Event of Default is referred to in paragraph (a), (b), (c), (d) or (e) of Section 6.2, any or all of such remedies concurrently with the exercise and pursuit by the Owner Trustee of any or all of the remedies then available to the Owner Trustee under the Facility Lease.

(b) Any provisions of the Facility Lease or this Indenture to the contrary notwithstanding, if the Lessee shall fail to pay any Excepted Payment to any Person entitled thereto as and when due, such Person shall have the right at all times, to the exclusion of the Indenture Trustee, to demand, collect, sue for, enforce performance of obligations relating to, or otherwise obtain all amounts due in respect of, such Excepted Payment.

SECTION 6.4. Specific Remedies; Enforcement of Claims without Possession of Notes.

Subject to Sections 6.2, 6.3 and 6.11 and the terms of the documents constituting a part of the Lease Indenture Estate, upon the occurrence and during the continuance of an Indenture Event of Default:

(a) The Indenture Trustee may, and upon receipt of a Directive shall, in order to enforce the rights of the Indenture Trustee and of the Holders of the Notes, direct payment to it of all moneys and enforce any agreement or undertaking constituting a part of the Lease Indenture Estate by any action, suit, remedy or proceeding authorized or permitted by this Indenture or by law or by equity, and whether for the specific performance of any agreement contained herein, or for an injunction against the violation of any of the terms hereof, or in aid of the exercise of any power granted hereby or by Applicable Law, and in addition may sell, assign, transfer and deliver, from time to time to the extent permitted by Applicable Law, all or any part of the Lease Indenture Estate or any interest therein, at any private sale or public auction with or without demand, advertisement or notice (except as herein required or as may be required by Applicable Law) of the date, time and place of sale and any adjournment thereof, for cash or credit or other property, for immediate or future delivery and for such price or prices and on such terms as the Indenture Trustee, in its uncontrolled discretion, may determine, or as may be required by Applicable Law, so long as the Equity Participant and the Owner Trustee are afforded a commercially reasonable opportunity to bid for all or such part of the Lease Indenture Estate in connection therewith. It is agreed that 90 days' notice to the Equity Participant, the Owner Trustee and the Lessee of the date, time and place of any proposed sale by the Indenture Trustee of all or any part of the Lease Indenture Estate or interest therein is reasonable. The Indenture Trustee may file such proofs of claim and other papers or documents as may be necessary or advisable in order to have the claims of the Indenture Trustee and of the Holders of the Notes asserted or upheld in any bankruptcy, receivership or other judicial proceedings. To the extent that any portion of the Lease Indenture Estate constitutes fixtures or real property, the Indenture Trustee shall have, to the extent not inconsistent with this Indenture, all the rights, remedies and benefits of a mortgagee of real property under Applicable Law

(including, without limitation, rights and remedies pursuant to Arizona Revised Statutes Section 33 - 702.B, or any comparable successor provision).

(b) Without limiting the foregoing, the Indenture Trustee, its assigns and its legal representatives, subject to the rights of the Lessee under the Facility Lease, shall have as to such of the Lease Indenture Estate as is subject to the Uniform Commercial Code or similar law in each relevant jurisdiction all the remedies of a secured party under the Uniform Commercial Code or similar law in such jurisdiction and such further remedies as from time to time may hereafter be provided in such jurisdiction for a secured party.

(c) All rights of action and rights to assert claims under this Indenture or under any of the Notes may be enforced by the Indenture Trustee without the possession of the Notes at any trial or other proceedings instituted by the Indenture Trustee, and any such trial or other proceedings shall be brought in its own name as trustee of an express trust, and any recovery or judgment shall be for the ratable benefit of the Holders of the Notes as herein provided. In any proceedings brought by the Indenture Trustee (and also any proceedings involving the interpretation of any provision of this Indenture to which the Indenture Trustee shall be a party) the Indenture Trustee shall be held to represent all the Holders of the Notes, and it shall not be necessary to make any such Holders parties to such proceedings.

(d) The Indenture Trustee may exercise any other right or remedy that may be available to it under Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(e) The Indenture Trustee agrees that the rights and remedies of the Indenture Trustee in the Undivided Interest, including the related Generation Entitlement Share, and, through the Real Property Interest, in the PVNGS Site are subject and subordinate to the rights and remedies of the ANPP Participants (other than (i) the Lessee or (ii) any Person who shall become an ANPP Participant in respect of the Lessor's Interest) under the ANPP Project Agreement.

(f) The Indenture Trustee agrees that, except as provided in Sections 15.2.2, 15.6.4 and 15.10 (or any

comparable successor provisions) of the ANPP Participation Agreement, the Lessee shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Owner Trustee and the Indenture Trustee) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of the Lessee transferred to the Owner Trustee pursuant to the Transaction Documents.

SECTION 6.5. Rights and Remedies Cumulative.

Subject to Sections 6.2, 6.3 and 6.11, (a) each and every right, power and remedy herein specifically given to the Indenture Trustee under this Indenture shall be cumulative and shall be in addition to every other right, power and remedy herein specifically given or now or hereafter existing at law, in equity or by statute, and each and every right, power and remedy whether specifically herein given or otherwise existing may be exercised from time to time and as often and in such order as may be deemed expedient by the Indenture Trustee, and the exercise or the beginning of the exercise of any right, power or remedy shall not be construed to be a waiver of the right to exercise at the same time or thereafter any other right, power or remedy, and (b) no delay or omission by the Indenture Trustee in the exercise of any right, power or remedy or in the pursuance of any remedy shall impair any such right, power or remedy or be construed to be a waiver of any default on the part of the Equity Participant, the Owner Trustee or the Lessee or to be an acquiescence therein.

SECTION 6.6. Restoration of Rights and Remedies.

In case the Indenture Trustee shall have proceeded to enforce any right, power or remedy under this Indenture by foreclosure, entry or otherwise, and such proceedings shall have been discontinued or abandoned for any reason or shall have been determined adversely to the Indenture Trustee, then and in every such case the Owner Trustee, the Equity Participant, the Indenture Trustee and the Lessee shall be restored to their former positions and rights hereunder with respect to the Lease Indenture Estate, and all rights, powers and remedies of the Indenture Trustee shall continue as if no such proceedings had been taken.

SECTION 6.7. Waiver of Past Defaults.

Any past Indenture Default or Indenture Event of Default and its consequences may be waived by the Indenture Trustee, except an Indenture Default or an Indenture Event of Default (i) in the payment of the principal of or premium, if any, or interest on any Note, subject to the provisions of Section 7.1, or (ii) in respect of a covenant or provision hereof which, under Section 10.2, cannot be modified or amended without the consent of each Holder of a Note then Outstanding. Upon any such waiver, such Indenture Default or Indenture Event of Default shall cease to exist, and any other Indenture Event 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 Indenture Default or Indenture Event of Default or impair any right consequent thereon.

SECTION 6.8. Right of Owner Trustee to Pay Rent; Note Purchase; Substitute Lessee.

Anything in this Article VI or Article VII to the contrary notwithstanding:

(a) an Indenture Event of Default shall be deemed cured if such Indenture Event of Default results from non-payment of Basic Rent or Supplemental Rent under the Facility Lease, and the Owner Trustee or the Equity Participant shall have paid all principal of and interest on the Notes due (other than by acceleration) on the date such Basic Rent was payable (plus interest on such amount as required hereby) within 15 days after the receipt by the Owner Trustee of notice of such non-payment, such receipt to be evidenced by, among other things, any notice thereof given to the Owner Trustee in accordance with the notice provisions of the Participation Agreement; provided, however, that (1) during the period that any Initial Series Notes are Outstanding, the Owner Trustee shall not be permitted to exercise its right to cure Indenture Events of Default under this clause (a) with respect to more than twelve consecutive dates on which Basic Rent is due and 24 such dates in the aggregate, and (2) during the period that the Refunding Notes are Outstanding, the Owner Trustee shall not be permitted to exercise its rights to cure Indenture Events of Default under this clause (a) with respect to more than two consecutive Basic Rent Payment Dates or on more than four Basic Rent Payment Dates

during the Lease Term. The Owner Trustee or the Equity Participant, upon exercising cure rights under this paragraph (a), shall not obtain any Lien on any part of the Lease Indenture Estate on account of such payment for the costs and expenses incurred in connection therewith nor, except as expressly provided in the succeeding sentence, shall any claims of the Owner Trustee or the Equity Participant against the Lessee or any other Person for the repayment thereof impair the prior right and security interest of the Indenture Trustee in and to the Lease Indenture Estate. Upon any payment by the Owner Trustee or the Equity Participant pursuant to this Section 6.8, the Owner Trustee or the Equity Participant, as the case may be, shall (to the extent of such payment made by it) be subrogated to the rights of the Indenture Trustee and the Holders of the Notes to receive the payment of Rent with respect to which the Owner Trustee or the Equity Participant made such payment and interest on account of such Rent payment being overdue in the manner set forth in the next sentence. If the Indenture Trustee shall thereafter receive such payment of Rent or such interest, the Indenture Trustee shall, notwithstanding the requirements of Section 5.1, on the date such payment is received by the Indenture Trustee, remit such payment of Rent (to the extent of the payment made by the Owner Trustee or the Equity Participant pursuant to this Section 6.8) and such interest to the Owner Trustee or the Equity Participant, as the case may be, in reimbursement for the funds so advanced by it, provided that if (i) any Indenture Event of Default hereunder shall have occurred and be continuing such payment shall not be remitted to the Owner Trustee or the Equity Participant but shall be held by the Indenture Trustee as security for the obligations secured hereby and distributed in accordance with Section 5.1 hereof, as appropriate, and provided, further that if the principal of and interest on the Notes shall have become due and payable pursuant to Section 7.1 hereof, such Rent and interest thereon shall be distributed by the Indenture Trustee in the order of priority set forth in Section 5.3 hereof.

(b) Each Holder of a Note agrees, by acceptance thereof, that if the Notes have been accelerated pursuant to Section 7.1, and the Owner Trustee, within 30 days after receiving notice from the Indenture Trustee pursuant to Section 7.1, shall give written notice to the Indenture Trustee of the Owner Trustee's intention to purchase all of the Notes in accordance with this paragraph, accompanied by assurances of the

Owner Trustee to purchase the Notes, then, upon receipt within 10 Business Days after such notice from the Owner Trustee of an amount equal to the aggregate unpaid principal amount of and any premium with respect to any unpaid Notes then held by such Holder, together with accrued but unpaid interest thereon to the date of such receipt (as well as any interest on overdue principal and, to the extent permitted by law, interest), such Holder will forthwith sell, assign, transfer and convey to the Owner Trustee (without recourse or warranty of any kind other than of title to the Notes so conveyed) all of the right, title and interest of such Holder in and to the Lease Indenture Estate, this Indenture and all Notes held by such Holder; provided, that no such Holder shall be required so to convey unless (1) the Owner Trustee shall have simultaneously tendered payment for all other Notes issued by the Owner Trustee at the time Outstanding pursuant to this paragraph and (2) such conveyance is not in violation of any Applicable Law.

(c) Each Holder of a Note further agrees by its acceptance thereof that the Owner Trustee shall have the right, pursuant to Section 16 of the Facility Lease, to terminate the Facility Lease and, in connection therewith, to arrange for the substitution of another Person as lessee under a new lease substantially similar to, and containing terms no less favorable to the Holders of the Notes than the terms of, the Facility Lease (hereinafter the Substituted Lessee) and, subject to: (i) any Indenture Event of Default under paragraphs (f), (g), (h), (i), (j) or (k) of Section 6.2 having been cured by the Owner Trustee, (ii) the Substituted Lessee's assuming all of the obligations under the Facility Lease and the Indenture Trustee having been provided with an opinion of counsel to the effect that the Substituted Lessee's assumption thereof is the valid and binding obligation of the Substituted Lessee and that no Governmental Actions (other than such as have been obtained) are required in connection with the Substituted Lessee's performance of the Facility Lease and (iii) the Substituted Lessee's having an assigned credit rating by Standard & Poor's Corporation and Moody's Investors Service, Inc. (or, if either of such organizations shall not rate securities issued by such Substituted Lessee, by any other nationally recognized rating organization in the United States of America) with respect to at least one series of its debt obligations or preferred stock equal to or better than the ratings assigned, immediately prior to such substitution, by such organizations to comparable

securities of the Lessee immediately prior to such substitution but in no event less than "investment grade" rating assigned by such organizations, the Facility Lease between the Owner Trustee and such Substituted Lessee shall, for all purposes of this Indenture, be deemed to be the Facility Lease subject to the lien of this Indenture.

SECTION 6.9. Further Assurances.

Subject to Section 7.6, the Owner Trustee covenants and agrees from time to time to do all such acts and execute all such instruments of further assurance as shall be reasonably requested by the Indenture Trustee for the purpose of fully carrying out and effectuating this Indenture and the intent hereof.

SECTION 6.10. Right of Indenture Trustee To Perform Covenants, etc.

If the Owner Trustee shall fail to make any payment or perform any act required to be made or performed by it hereunder or under the Facility Lease or if the Owner Trustee shall fail to release any Lien affecting the Lease Indenture Estate which it is required to release by the terms of this Indenture, the Indenture Trustee, without notice to or demand upon the Owner Trustee and without waiving or releasing any obligation or default, may (but shall be under no obligation to) at any time thereafter make such payment or perform such act for the account and at the expense of the Lease Indenture Estate. All sums so paid by the Indenture Trustee and all costs and expenses (including without limitation reasonable fees and expenses of legal counsel and other professionals) so incurred, together with interest thereon from the date of payment or occurrence, shall constitute additional indebtedness secured by this Indenture and shall be paid from the Lease Indenture Estate to the Indenture Trustee on demand. The Indenture Trustee shall not be liable for any damages resulting from any such payment or action unless such damages shall be a consequence of willful misconduct or gross negligence on the part of the Indenture Trustee.

SECTION 6.11. Certain Other Rights of the Owner Trustee.

(a) Except as otherwise provided in this Section 6.11, but notwithstanding any provision to the contrary in this Indenture, the Owner Trustee shall at

all times (other than during the period that the Indenture Trustee is entitled to exercise rights and powers and pursue remedies as provided in clause (x) of Section 6.3(a)) retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default, subject, however, to Section 10.2; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree to any amendment to, or any waiver, discharge or termination of, any term or provision of Sections 2(c), 3(g), 4, 7, 8(f)(iv), 9(i), 11, 15(i)(x), (i)(y), (vii) and (x) and the provisions affecting redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease.

(b) In the event that an Indenture Event of Default shall have occurred and be continuing, the Owner Trustee shall consult with the Indenture Trustee as to any proposed exercise or pursuit of remedies and the Indenture Trustee shall have the right, in its sole discretion, to cause the Owner Trustee to forbear from any such proposed action if the Indenture Trustee shall have determined that such action would have a material adverse effect on the Holders of the Notes ; provided, however, that the Owner Trustee shall not exercise or pursue remedies in a manner which would unreasonably deprive the Holders of the Notes of a material right or remedy unless the Owner Trustee is commensurately adversely affected.

Notwithstanding any provision of this Section 6.11 (other than Section 6.11(c)) to the contrary, the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the Stated Price) and (iii) the Owner Trustee shall not have notified the

Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date specified in the Owner Trustee's notice of election, to purchase within 60 days after the date of such notice of election to purchase. If the Owner Trustee shall fail to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate at a price no lower than the Stated Price to any Person (other than the Indenture Trustee or a Holder or Holders of more than 25% of the Outstanding Bonds or Notes (including in each case Affiliates thereof)) at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the purchase price for the Lease Indenture Estate, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate.

(c) Notwithstanding any provision of this Indenture (including Section 6.11(b)) to the contrary, in no event shall the exercise of rights, powers and remedies by the Indenture Trustee cause the Owner Trustee to be in violation of Applicable Law nor shall the pursuit of such remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee (as defined in the ANPP Participation Agreement).

ARTICLE VII

CERTAIN DUTIES OF THE OWNER TRUSTEE AND THE INDENTURE TRUSTEE

SECTION 7.1. Duties in Respect of Events of Default, Deemed Loss Events and Events of Loss; Acceleration of Maturity.

In the event the Owner Trustee shall have actual knowledge of an Indenture Event of Default, an Event of Default, a Deemed Loss Event or an Event of Loss, the Owner Trustee shall give prompt written notice thereof to the Equity Participant, the Lessee and the Indenture Trustee. In the event the Indenture Trustee

shall have actual knowledge of an Event of Default, an Indenture Event of Default, a Deemed Loss Event or an Event of Loss, the Indenture Trustee shall give prompt written notice thereof to the Equity Participant, the Owner Trustee, the Lessee and each Holder of a Note. Subject to the terms of Sections 6.2, 6.3, 6.4, 6.8, 6.11 and 7.3, (a) the Indenture Trustee shall take such action (including the waiver of past Defaults in accordance with Section 6.7), or refrain from taking such action, with respect to any such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss as the Indenture Trustee shall be instructed by a Directive, (b) if the Indenture Trustee shall not have received instructions as above provided within 20 days after mailing by the Indenture Trustee of notice of such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss to the Persons referred to above, the Indenture Trustee may, subject to instructions thereafter received pursuant to the preceding sentence, take such action, or refrain from taking such action, but shall be under no duty to take or refrain from taking any action, with respect to such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss as it shall determine advisable in the best interests of the Holders of the Notes of all series and (c) in the event that an Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee in its discretion may, or upon receipt of a Directive shall, by written notice to the Owner Trustee, declare the unpaid principal amount of all Notes with accrued interest thereon to be immediately due and payable, upon which declaration such principal amount and such accrued interest shall immediately become due and payable without further act or notice of any kind. For all purposes of this Indenture, in the absence of actual knowledge, neither the Owner Trustee nor the Indenture Trustee shall be deemed to have knowledge of an Indenture Event of Default or Event of Default except that the Indenture Trustee shall be deemed to have knowledge of the failure of the Lessee to pay any installment of Basic Rent within 5 Business Days after the same shall become due. For purposes of this Section 7.1, neither the Owner Trustee nor the Indenture Trustee shall be deemed to have actual knowledge of any Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss unless it shall have received notice thereof pursuant to Section 11.6 or such Indenture Event of Default or Event of Default shall actually be known by an officer in the corporate trust department of the Owner Trustee or by an officer in the

Corporate Trustee Administration Department of the Indenture Trustee, as the case may be.

SECTION 7.2. Duties in Respect of Matters Specified in Directive.

Subject to the terms of Sections 6.2, 6.3, 6.4, 6.8, 6.11, 7.1 and 7.3, upon receipt of a Directive, the Indenture Trustee shall take such of the following actions as may be specified in such Directive: (i) give such notice or direction or exercise such right, remedy or power permitted hereunder or permitted with respect to the Facility Lease or in respect of any part or all of the Lease Indenture Estate as shall be specified in such Directive; and (ii) take such action to preserve or protect the Lease Indenture Estate as shall be specified in such Directive, it being agreed that without such a Directive, the Indenture Trustee shall not waive, consent to or approve any such matter as satisfactory to it.

SECTION 7.3. Indemnification.

The Indenture Trustee shall not be required to take or refrain from taking any action under Section 7.1 or 7.2 or Article VI which shall require the Indenture Trustee to expend or risk its own funds or otherwise incur any financial liability unless the Indenture Trustee shall have been indemnified by the Holders of the Notes against liability, cost or expense (including counsel fees) which may be incurred in connection therewith, or unless, in the reasonable judgment of the Indenture Trustee, the indemnities of the Lessee shall be adequate for such purpose; provided, however, that if the Holder of such Notes is the Collateral Trust Trustee, the unsecured written undertaking of the Collateral Trust Trustee, in its individual capacity, shall be sufficient indemnity for purposes of this Section. The Indenture Trustee shall not be required to take any action under Section 7.1 or 7.2 or Article VI nor shall any other provision of this Indenture be deemed to impose a duty on the Indenture Trustee to take any action, if the Indenture Trustee shall reasonably determine, or shall have been advised by counsel, that such action is likely to result in personal liability or is contrary to the terms hereof or of the Facility Lease or is otherwise contrary to law.

SECTION 7.4. Limitations on Duties; Discharge of Certain Liens Resulting from Claims Against Indenture Trustee.

The Indenture Trustee shall have no duty or obligation to take or refrain from taking any action under, or in connection with, this Indenture or the Facility Lease, except as expressly provided by the terms of this Indenture. The Indenture Trustee nevertheless agrees that it will, in its individual capacity and at its own cost and expense, promptly take such action as may be necessary duly to discharge all Liens on any part of the Lease Indenture Estate which result from acts by or claims against it arising out of events or conditions not related to its rights in the Lease Indenture Estate or the administration of the Lease Indenture Estate or the transactions contemplated hereby.

SECTION 7.5. Restrictions on Dealing with Lease Indenture Estate.

Except as provided in the Transaction Documents, the Owner Trustee shall not use, operate, store, lease, control, manage, sell, dispose of or otherwise deal with any part of the Lease Indenture Estate.

SECTION 7.6. Filing of Financing Statements and Continuation Statements.

Pursuant to Section 10(b)(2) of the Participation Agreement, the Lessee has covenanted to maintain the priority of the lien of this Indenture on the Lease Indenture Estate. The Indenture Trustee shall, at the request and expense of the Lessee as provided in the Participation Agreement, execute and deliver to the Lessee and the Lessee will file, if not already filed, such financing statements or other documents and such continuation statements or other documents with respect to financing statements or other documents previously filed relating to the lien created under this Indenture in the Lease Indenture Estate as may be necessary to protect, perfect and preserve the lien created under this Indenture. At any time and from time to time, upon the request of the Lessee or the Indenture Trustee, at the expense of the Lessee as provided in the Participation Agreement (and upon receipt of the form of document so to be executed), the Owner Trustee shall promptly and duly execute and deliver any

and all such further instruments and documents as the Lessee or the Indenture Trustee may request in order for the Indenture Trustee to obtain the full benefits of the lien, security interest and assignment created or intended to be created hereby and of the rights and powers herein granted. Upon the reasonable instructions (which instructions shall be accompanied by the form of document to be filed) at any time and from time to time of the Lessee or the Indenture Trustee, the Owner Trustee shall execute and file any financing statement (and any continuation statement with respect to any such financing statement), any certificate of title or any other document, in each case relating to the lien, security interest and assignment created by this Indenture, as may be specified in such instructions. In addition, the Indenture Trustee and the Owner Trustee will execute such continuation statements with respect to financing statements and other documents relating to the lien created under this Indenture in the Lease Indenture Estate as may be reasonably specified from time to time in written instructions of any Holder of a Note (which instructions may, by their terms, be operative only at a future date and which shall be accompanied by the form of such continuation statement or other document so to be filed).

ARTICLE VIII

CONCERNING THE OWNER TRUSTEE AND THE INDENTURE TRUSTEE

SECTION 8.1. Acceptance of Trusts; Standard of Care.

The Indenture Trustee accepts the trusts hereby created and applicable to it and agrees to perform the same but only upon the terms of this Indenture and the Participation Agreement and agrees to receive and disburse all moneys constituting part of the Lease Indenture Estate in accordance with the provisions hereof, but no implied duties or obligations shall be read into this Indenture or the Participation Agreement against the Indenture Trustee. The Indenture Trustee shall enter into and perform its obligations under the Participation Agreement, and, at the request of the Owner Trustee, any other agreement relating to any transfer of the Undivided Interest or the Real Property

Interest or the assignment of rights under the Assignment and Assumption or, at the request of the Owner Trustee, the purchase by any Person of Notes or Additional Notes issued hereunder, all as contemplated hereby. The Indenture Trustee shall not be liable under any circumstances, except for its own willful misconduct or gross negligence. If any Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee shall exercise such of the rights and remedies vested in it by this Indenture, subject to the provisions hereof, and shall use the same degree of care in their exercise as a prudent man would exercise or use in the circumstances in the conduct of his own affairs, but if in the opinion of the Indenture Trustee such action may tend to involve expense or liability, it shall not be obligated to take such action unless it is furnished with indemnity satisfactory to it.

SECTION 8.2. No Duties of Maintenance, Etc.

Except pursuant to Section 7.2 and except as provided in, and without limiting the generality of, Sections 7.1 and 7.4, the Indenture Trustee shall have no duty (i) to see to any recording or filing of any Transaction Document, or to see to the maintenance of any such recording or filing, or (ii) to see to the payment or discharge of any tax, assessment or other governmental charge or any lien or encumbrance of any kind owing with respect to, or assessed or levied against, any part of the Lease Indenture Estate (except such as are required to be paid or discharged by it pursuant to this Indenture or any of the other Transaction Documents) or to make or file any reports or returns related thereto.

SECTION 8.3. Representations and Warranties of Indenture Trustee and the Owner Trustee.

NONE OF THE OWNER TRUSTEE, THE INDENTURE TRUSTEE OR THE EQUITY PARTICIPANT MAKES ANY REPRESENTATION OR WARRANTY AS TO THE VALUE, CONDITION, MERCHANTABILITY OR FITNESS FOR USE OF UNIT 2, THE UNDIVIDED INTEREST OR ANY PART OF THE LEASE INDENTURE ESTATE OR AS TO ITS INTEREST THEREIN, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO UNIT 2, THE UNDIVIDED INTEREST OR ANY PART OF THE LEASE INDENTURE ESTATE WHATSOEVER. The Owner Trustee and the Indenture Trustee each represents and warrants, in its individual capacity, as to itself that this Indenture has been executed and delivered by one or more of its officers who are duly

authorized to execute and deliver this Indenture on its behalf.

**SECTION 8.4. Moneys Held in Trust;
Non-Segregation of Moneys.**

All moneys and securities deposited with and held by the Indenture Trustee under this Indenture for the purpose of paying, or securing the payment of, the principal of or premium or interest on the Notes shall be held in trust. Except as provided in Sections 2.4(c), 8.8 and 11.1, moneys received by the Indenture Trustee under this Indenture need not be segregated in any manner except to the extent required by law, and may be deposited under such general conditions as may be prescribed by law; provided, however, that any payments received or applied hereunder by the Indenture Trustee shall be accounted for by the Indenture Trustee so that any portion thereof paid or applied pursuant hereto shall be identifiable as to the source thereof. Except as otherwise expressly provided herein, the Indenture Trustee shall not be liable for any interest on any money held pursuant to this Indenture.

SECTION 8.5. Reliance on Writings, Use of Agents, Etc.

The Indenture Trustee shall incur no liability to anyone in acting upon any signature, instrument, notice, resolution, request, consent, telegram, order, certificate, report, opinion, bond or other document or paper believed by it to be genuine and believed by it to be signed by the proper party or parties. In the case of the Lessee, the Indenture Trustee may accept a copy of a resolution of the Board of Directors or any duly constituted and authorized committee of the Board of Directors of the Lessee, certified by the Secretary or an Assistant Secretary of the Lessee as duly adopted and in full force and effect, as conclusive evidence that such resolution has been duly adopted by such Board or Committee and that the same is in full force and effect. As to the aggregate unpaid principal amount of the Notes Outstanding as of any date, the Owner Trustee may for all purposes hereof rely on a certificate signed by any Authorized Officer of the Indenture Trustee. As to any fact or matter the manner of ascertainment of which is not specifically described herein, the Indenture Trustee may for all purposes hereof rely on a certificate, signed by the Chairman of the Board, the President, any Vice President and the Treasurer or the

Secretary or any Assistant Treasurer or Assistant Secretary of the Lessee, or a Holder of a Note or any Responsible Officer of the Owner Trustee, as the case may be, as to such fact or matter, and such certificate shall constitute full protection to the Indenture Trustee for any action taken or omitted to be taken by it in good faith in reliance thereon. The Indenture Trustee shall furnish to the Owner Trustee upon request such information and copies of such documents as the Indenture Trustee may have and as are necessary for the Owner Trustee to perform its duties under Article III. In the administration of the trusts hereunder, the Indenture Trustee may execute any of the trusts or powers hereof and perform its powers and duties hereunder directly or through agents or attorneys selected by it in good faith and with reasonable care, and, with respect to matters relating to the Notes, the Lease Indenture Estate and its rights and duties under this Indenture and the other Transaction Documents, may, at the expense of the Lessee, or, if the Lessee shall have failed to pay or provide for the payment thereof, at the expense of the Lease Indenture Estate; consult with counsel, accountants and other skilled persons to be selected and employed by it in good faith and with reasonable care, and the Indenture Trustee shall not be liable for anything done, suffered or omitted in good faith by it in accordance with the advice or opinion of any such counsel, accountants or other skilled persons so selected. Unless otherwise specified herein or in any other Transaction Document, any opinion of counsel referred to in this Indenture or in such other Transaction Document may be relied on by the Indenture Trustee to the extent it is rendered by an attorney or firm of attorneys satisfactory to the Indenture Trustee (which may be counsel to the Equity Participant, the Owner Trustee, the Lessee or any party to any Transaction Document).

SECTION 8.6. Indenture Trustee to Act Solely as Trustee.

The Indenture Trustee acts hereunder solely as trustee as herein provided and not in any individual capacity, except as otherwise expressly provided herein; and except as provided in Sections 9(a) and 9(b) of the Participation Agreement or Section 7.4 or 8.1, all Persons having any claim against the Indenture Trustee arising from matters relating to the Notes by reason of the transactions contemplated hereby shall, subject to the lien and priorities of payment as herein provided

and to Sections 3.6 and 5.7, look only to the Lease Indenture Estate for payment or satisfaction thereof.

SECTION 8.7. Limitation on Rights Against Registered Holders, the Owner Trustee or Lease Indenture Estate.

The Indenture Trustee shall be entitled to be paid or reimbursed for Trustee's Expenses as provided herein and in the other Transaction Documents. Nonetheless, the Indenture Trustee agrees that it shall have no right against the Holders of the Notes, the Owner Trustee (except to the extent included in Transaction Expenses payable by the Equity Participant) or, except as provided in Article V and Section 6.4 or this Article VIII, the Lease Indenture Estate for any fee as compensation for its services hereunder.

SECTION 8.8. Investment of Certain Payments Held by the Indenture Trustee.

Any amounts held by the Indenture Trustee hereunder other than pursuant to Section 2.3(c) or 11.1 shall be invested by the Indenture Trustee from time to time as directed in writing by the Owner Trustee or by the Equity Participant as agent of the Owner Trustee and at the expense and risk of the Equity Participant in (i) obligations of, or guaranteed as to interest and principal by, the United States Government maturing not more than 90 days after such investment, (ii) open market commercial paper of any corporation incorporated under the laws of the United States of America or any State thereof rated "prime-1" or its equivalent by Moody's Investors Service, Inc. or "A-1" or its equivalent by Standard & Poor's Corporation or (iii) certificates of deposit maturing within 90 days after such investment issued by commercial banks organized under the laws of the United States of America or of any political subdivision thereof having a combined capital and surplus in excess of \$500,000,000; provided, however, that the aggregate amount at any one time so invested (a) in open market commercial paper of any corporation shall not exceed \$2,000,000 and (b) in certificates of deposit issued by any one bank shall not exceed \$10,000,000. Any income or gain realized as a result of any such investment shall be applied to make up any losses resulting from any such investment to the extent such losses shall not have been paid by the Owner Trustee or the Equity Participant pursuant to this Section 8.8. Any further income or gain so realized

shall be promptly distributed (in no event later than the next Business Day) to the Owner Trustee or the Equity Participant, except after the occurrence and during the continuance of an Indenture Event of Default. The Indenture Trustee shall have no liability for any loss resulting from any investment made in accordance with this Section. Any such investment may be sold (without regard to maturity date) by the Indenture Trustee whenever necessary to make any distribution required by Article V.

SECTION 8.9. No Responsibility for Recitals, etc.

The Indenture Trustee makes no representation or warranty as to the correctness of any statement, recital or representation made by any Person other than the Indenture Trustee in this Indenture, any other Transaction Document or the Notes.

SECTION 8.10. Indenture Trustee May Engage in Certain Transactions.

The Indenture Trustee may engage in or be interested in any financial or other transaction with the Lessee, the Equity Participant, the Owner Trustee and any other party to a Transaction Document, provided that if the Indenture Trustee determines that any such relation is in conflict with its duties under this Indenture, it shall eliminate the conflict or resign as Indenture Trustee.

SECTION 8.11. Construction of Ambiguous Provisions.

The Indenture Trustee, subject to Section 8.1, may construe any ambiguous or inconsistent provisions of this Indenture, and any such construction by the Indenture Trustee shall be binding upon the Noteholders. In construing any such provision, the Indenture Trustee will be entitled to rely upon opinions of counsel and will not be responsible for any loss or damage resulting from reliance in good faith thereon, except for its own gross negligence or willful misconduct.

ARTICLE IX

SUCCESSOR TRUSTEES

SECTION 9.1. Appointment of Co-Trustees or Separate Trustees.

(a) At any time or times, when necessary or prudent or for the purpose of meeting the legal requirements of any jurisdiction in which any part of the Lease Indenture Estate may, at any time, be located, the Indenture Trustee, except as set forth in subsection (b)(6) of this Section 9.1, may, and upon receipt of a Directive shall, appoint one or more Persons to act as co-trustee of all or any such part of the Lease Indenture Estate or to act as separate trustee of any property constituting part thereof, in either case with such powers as may be provided in the instrument of appointment, and to vest in such Person or Persons any property, title, right or power deemed necessary or desirable, subject to the remaining provisions of this Section 9.1. Except as set forth in subsection (b)(6) of this Section 9.1 the Owner Trustee shall join in any such appointment upon the request of the Indenture Trustee, but such joining will not be necessary for the effectiveness of such appointment.

(b) Every separate trustee or co-trustee shall be appointed subject to the following terms:

(1) The rights, powers, duties and obligations conferred or imposed upon any such separate trustee or co-trustee shall not be greater than those conferred or imposed upon the Indenture Trustee, and such rights and powers shall be exercisable only jointly with the Indenture Trustee, except to the extent that, under any law of any jurisdiction in which any particular act or acts are to be performed, the Indenture Trustee shall be incompetent or unqualified to perform such act or acts, in which event, except as set forth in subsection (b)(6) of this Section 9.1, such rights and powers shall be exercised by such separate trustee or co-trustee subject to the provisions of subsection (b)(4) of this Section 9.1.

(2) The Indenture Trustee may at any time, by an instrument in writing executed by it, accept the resignation of, and may (and upon the receipt of a Directive, shall) remove any separate trustee or co-trustee appointed under this Section 9.1.

(3) No trustee, including the Indenture Trustee, under this Indenture shall be liable by reason of any act or omission of any other trustee or co-trustee under this Indenture.

(4) Except as set forth in subsection (b) (6) of this Section 9.1, no power given to such separate trustee or co-trustee shall be separately exercised hereunder by such separate trustee or co-trustee except with the consent in writing of the Indenture Trustee.

(5) The Indenture Trustee shall maintain custody of all money and securities:

(6) Notwithstanding anything contained to the contrary in this Section 9.1, to the extent the laws of any jurisdiction preclude the Indenture Trustee from taking any action hereunder either alone, jointly or through a separate trustee under the direction and control of the Indenture Trustee, the Owner Trustee, at the instruction of the Indenture Trustee, shall appoint a separate trustee for such jurisdiction, which separate trustee shall have full power and authority to take all action hereunder as to matters relating to such jurisdiction without the consent of the Indenture Trustee, but subject to the same limitations in any exercise of his power and authority as those to which the Indenture Trustee is subject.

(c) Upon the acceptance in writing of such appointment by any such separate trustee or co-trustee, it shall be vested with the estates or property to which its appointment relates as specified in the instrument of appointment, subject to all the terms of this Indenture.

(d) Any separate trustee or co-trustee may, at any time, constitute the Indenture Trustee, its agent or attorney-in-fact, with full power and authority, to the

extent not prohibited by law, to do any lawful act under or in respect of this Indenture on its behalf and in its name. If a separate trustee or co-trustee shall die, become incapable of acting, resign or be removed, all of its estates, properties, rights, remedies and trusts shall vest in and be exercised by the Indenture Trustee, to the extent permitted by law, without the appointment of a new or successor trustee.

SECTION 9.2. Resignation and Removal of Indenture Trustee; Appointment of Successor.

(a) The Indenture Trustee may resign at any time without cause by giving at least 30 days' prior written notice to the Equity Participant, the Owner Trustee, the Lessee and to each Holder of a Note, such resignation to be effective upon the acceptance of such trusteeship by a successor. In addition, the Indenture Trustee may be removed without cause by a Directive delivered to the Equity Participant, the Owner Trustee, the Lessee and the Indenture Trustee, and the Indenture Trustee shall promptly give notice thereof in writing to each Holder of a Note. In the case of the resignation or removal of the Indenture Trustee, a successor trustee may be appointed by such a Directive. If a successor trustee shall not have been appointed within 30 days after such notice of resignation or removal, the Indenture Trustee, the Owner Trustee or any Holder of a Note may apply to any court of competent jurisdiction to appoint a successor to act until such time, if any, as a successor shall have been appointed as above provided. The successor so appointed by such court shall immediately and without further act be superseded by any successor appointed as above provided within one year from the date of the appointment by such court.

(b) Any successor trustee, however appointed, shall execute and deliver to its predecessor and to the Owner Trustee an instrument accepting such appointment, and thereupon such successor, without further act, shall become vested with all the estates, properties, rights, powers and duties of its predecessor hereunder in the trusts under this Indenture applicable to it with like effect as if originally named the Indenture Trustee; but, nevertheless, upon the written request of such successor trustee or receipt of a Directive, its predecessor shall execute and deliver an instrument transferring to such successor trustee, upon the trusts herein expressly applicable to it, all the estates, properties, rights and powers of such predecessor under this

Indenture, and such predecessor shall duly assign, transfer, deliver and pay over to such successor trustee all moneys or other property then held by such predecessor under this Indenture.

(c) Any successor trustee, however appointed, shall be a bank or trust company organized under the laws of the United States or any jurisdiction thereof having a combined capital and surplus of at least \$100,000,000, if there be such an institution willing, able and legally qualified to perform the duties of the Indenture Trustee hereunder upon reasonable or customary terms.

(d) Any corporation into which the Indenture 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 Indenture Trustee shall be a party, or any corporation to which substantially all the corporate trust business of the Indenture Trustee may be transferred, shall, subject to the terms of paragraph (c) of this Section 9.1, be the Indenture Trustee under this Indenture without further act.

ARTICLE X

SUPPLEMENTS AND AMENDMENTS TO THIS INDENTURE AND OTHER DOCUMENTS

SECTION 10.1. Supplements, Amendments and Modifications to This Indenture Without Consent of Holders of Notes.

The Indenture Trustee may, with the written consent of the Owner Trustee, from time to time and at any time execute a supplement to this Indenture without the consent of the Holders of Notes Outstanding in order to (i) cure any defect, omission or ambiguity in this Indenture or for any other purpose if such action does not adversely affect the interests of such Holders, (ii) grant or confer upon the Indenture Trustee for the benefit of such Holders any additional rights, remedies, powers, authority or security which may be lawfully granted or conferred and which are not contrary to or inconsistent with this Indenture, (iii) add to the covenants or agreements to be observed by the Owner

Trustee and which are not contrary to or inconsistent with this Indenture or surrender any right or power of the Owner Trustee, (iv) confirm or amplify, as further assurance, any pledge under, and the attachment of, or subjection to any lien, security interest or pledge created or to be created by, this Indenture, of the properties covered hereby, or subject to attachment of, or the lien, security interest or pledge of this Indenture additional revenues, properties or other collateral, (v) qualify this Indenture under the provisions of the Trust Indenture Act, (vi) evidence the appointment of any successor Indenture Trustee pursuant to the terms hereof, (vii) evidence the assumption and release affected by the Assumption Agreement, or (viii) execute supplemental indentures to evidence the issuance of and to provide the terms of, Additional Notes to be issued hereunder in accordance with the terms hereof.

SECTION 10.2. Supplements and Amendments to this Indenture and the Facility Lease With Consent of Holders of Notes.

Except as provided in Section 10.1, at any time and from time to time, (i) upon receipt of a Directive, the Indenture Trustee shall execute a supplement to this Indenture for the purpose of adding provisions to, or changing or eliminating provisions of, this Indenture or for the purpose of consenting to the amendment to or waiver of Sections 2(c), 7, 8(f)(iv), 9(i), 11, 15(i)(x), 15(vii), 15(x) and 16 of the Facility Lease, but only as specified in such Directive, and (ii) upon receipt of a written instruction from the Lessee and the Owner Trustee, the Indenture Trustee shall consent to any amendment of or supplement to any Granting Clause Document otherwise than as provided in the proviso to Section 6.11(a) or execute and deliver such written waiver or modification of the terms of any Granting Clause Document otherwise than as provided in the proviso to Section 6.11(a); provided, however, that, without the consent of the Holders of all the Notes then Outstanding no such supplement or amendment to this Indenture or any Granting Clause Document, or waiver or modification of the terms of either thereof, shall (w) modify, waive, discharge or terminate any of the provisions of this Section or of Section 3.5, 7.1 or 7.2, or Sections 3(g), 4, 15(i)(y), and 14 (insofar as it affects redemption of the Notes) of the Facility Lease or of the definition of Directive contained in Appendix A hereto or the definition of Indenture Event of Default herein, reduce the amount of the Basic Rent

or Casualty Value or any payment under or pursuant to Section 16 of the Facility Lease as set forth in the Facility Lease below such amount as is required to pay the full principal of, and premium, if any, and interest on, the Notes when due, or extend the time of payment thereof, (x) otherwise modify, amend or supplement the Facility Lease in such manner as to reduce the Lessee's obligations in respect of the payment of the Basic Rent or Casualty Value or any payment under or pursuant to Section 16 of the Facility Lease below the amount referred to in clause (w) above, (y) except as provided in this Indenture, deprive the Holder of any Note of the lien of this Indenture on the Lease Indenture Estate or (z) materially adversely affect the rights and remedies for the benefit of such Holder provided in Article VI; and, provided, further, that, without the consent of the Holders of all the Notes then Outstanding and affected thereby, no such supplement or amendment to this Indenture or the Facility Lease, or waiver or modification of the terms of either thereof, shall reduce the amount or extend the time of payment of any amount payable under any Note, reduce or modify the provisions for the computation of the rate of interest owing or payable thereon, adversely alter or modify the provisions of Article V with respect to the order of priorities in which distributions thereunder with respect to the Notes shall be made, or reduce, modify or amend any indemnities in favor of the Holders of the Notes. Anything to the contrary contained herein notwithstanding, without the necessity of the consent of the Holders of Notes or the Indenture Trustee, (a) any indemnities in favor of the Owner Trustee or the Equity Participant may be modified, amended or changed and (b) the Owner Trustee may enter into any agreement with respect to the Lease Indenture Estate which by its terms does not become effective prior to the satisfaction and discharge of this Indenture, but any agreement entered into by the Owner Trustee pursuant to this clause (b) shall not materially adversely affect the Indenture Trustee or the Holder of any Note. Notwithstanding the foregoing, the Indenture Trustee shall, upon receipt of a written instruction from the Lessee and the Owner Trustee, consent to an amendment of any definitions contained in or appended to this Indenture which are being changed pursuant to the amendments, if any, referred to in Section 10(b)(3)(xii) of the Participation Agreement. The Owner Trustee shall deliver to the Indenture Trustee a copy of each amendment to the Facility Lease whether or not the Indenture Trustee is required to consent or otherwise act with respect thereto.

SECTION 10.3. Certain Limitations on Supplements and Amendments.

If in the opinion of the Owner Trustee or the Indenture Trustee, each of which shall be entitled to rely on counsel for purposes of this Section 10.3, any document required to be executed by either of them pursuant to the terms of Section 10.1 or 10.2 does not comply with the provisions of this Indenture or adversely affects any right, immunity or indemnity in favor of, or increases any duty of, the Owner Trustee or the Indenture Trustee under this Indenture, the Facility Lease or the Participation Agreement, the Owner Trustee or the Indenture Trustee, as the case may be, may in its discretion decline to execute such document.

SECTION 10.4. Directive Need Not Specify Particular Form of Supplement or Amendment.

It shall not be necessary for any Directive furnished pursuant to Section 10.2 to specify the particular form of the proposed documents to be executed pursuant to such Section, but it shall be sufficient if such request shall indicate the substance thereof.

SECTION 10.5. Trustee to Furnish Copies of Supplement or Amendment.

Promptly after the execution by the Owner Trustee or the Indenture Trustee of any document entered into pursuant to Section 10.2; the Indenture Trustee shall mail, by first-class mail, postage prepaid, a conformed copy thereof to each Holder of an Outstanding Note at the address of such Person set forth in the register kept pursuant to Section 4.1 but the failure of the Indenture Trustee to mail such conformed copies shall not impair or affect the validity of such document.

ARTICLE XI

MISCELLANEOUS

SECTION 11.1. Moneys for Payments in Respect of Notes to be Held in Trust.

In case the Holder of any Note shall fail to present the same for payment on any date on which the principal thereof or interest thereon becomes payable, the Indenture Trustee may set aside in trust the moneys then due thereon uninvested and shall pay such moneys to the Holder of such Note or such Person upon due presentation or surrender thereof in accordance with the provisions of this Indenture, subject always, however, to the provisions of Sections 3.8 and 11.2.

SECTION 11.2. Disposition of Moneys Held for Payments of Notes.

Any moneys set aside under Section 11.1 and not paid to Holders of Notes as provided in Section 11.1 shall be held by the Indenture Trustee in trust until the latest of (i) the date three years after the date of such setting aside, (ii) the date all other Holders of the Notes shall have received full payment of all principal of and interest and other sums payable to them on such Notes or the Indenture Trustee shall hold (and shall have notified such Persons that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due and (iii) the date the Owner Trustee shall have fully performed and observed all its covenants and obligations contained in this Indenture with respect to the Notes; and thereafter shall be paid to the Owner Trustee by the Indenture Trustee on demand; and thereupon the Indenture Trustee shall be released from all further liability with respect to such moneys; and thereafter the Holders of the Notes in respect of which such moneys were so paid to the Owner Trustee shall have no rights in respect thereof except to obtain payment of such moneys from the Owner Trustee. Upon the setting aside of such moneys, interest shall cease to accrue on the Notes.

SECTION 11.3. Transfers Not to Affect Indenture or Trusts.

No Holder of a Note shall have legal title to any part of the Lease Indenture Estate. No transfer, by operation of law or otherwise, of any Note or other right, title and interest of any Holder of a Note in and to the Lease Indenture Estate or hereunder shall operate to terminate this Indenture or the trusts hereunder with respect to such Note or entitle any successor or transferee of such Holder to an accounting or to the transfer to it of legal title to any part of the Lease Indenture Estate.

SECTION 11.4. Binding Effect of Sale of Lease Indenture Estate.

Any sale or other conveyance of the Lease Indenture Estate or any part thereof by the Indenture Trustee made pursuant to the terms of this Indenture or the Facility Lease shall bind the Holders of the Notes and shall be effective to transfer or convey all right, title and interest of the Indenture Trustee, the Owner Trustee and such Holders in and to the same. No purchaser or other grantee shall be required to inquire as to the authorization, necessity, expediency or regularity of such sale or conveyance or as to the application of any sale or other proceeds with respect thereto by the Indenture Trustee.

SECTION 11.5. Limitation as to Enforcement of Rights, Remedies and Claims.

Nothing in this Indenture, whether express or implied, shall be construed to give to any Person, other than the Owner Trustee, the Equity Participant, the Lessee (to the extent the Lessee's consent or other action by the Lessee is expressly provided for), the Indenture Trustee and the Holders of the Notes, any legal or equitable right, remedy or claim under or in respect of this Indenture or any Note.

SECTION 11.6. Notices.

Unless otherwise expressly specified or permitted by the terms hereof, all communications and notices given hereunder to the Lessee, the Owner Trustee, the Equity Participant or the Indenture Trustee shall be given in the manner provided in Section 18 of the Participation Agreement. Notices by the Indenture

Trustee to any Holder of a Note shall be in writing, and shall be given in person or by means of telex, telecopy or other wire transmission (with request for assurance of receipt in a manner typical with respect to communications of that type), or mailed by registered or certified mail, addressed to such Holder at the address set forth in the register kept pursuant to Section 4.1. Whenever any notice in writing is required to be given by the Indenture Trustee to any Holder of a Note such notice shall be effective (x) if sent by telex, telecopy or other wire transmission, on the date of transmission thereof, or (y) if sent by mail, three Business Days after being mailed.

SECTION 11.7. Separability of Provisions

In case any one or more of the provisions of this Indenture or any application thereof shall be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions hereof and any other application hereof shall not in any way be affected or impaired.

SECTION 11.8. Benefit of Parties, Successors and Assigns.

All representations, warranties, covenants and agreements contained herein shall be binding upon, and inure to the benefit of, the Owner Trustee, the Indenture Trustee and their respective successors and assigns and each Holder of a Note, all as herein provided. Any request, notice, direction, consent, waiver or other instrument or action by any Holder of a Note shall bind the successors and assigns of such Holder and any Holder of a Note issued in transfer or exchange of such Note.

SECTION 11.9. Survival of Representations and Warranties.

All representations and warranties made with respect to the Notes shall survive the execution and delivery of this Indenture and the issue, sale and delivery of any Notes and shall continue in effect so long as any Note issued hereunder is Outstanding and unpaid.

SECTION 11.10. Bankruptcy of the Owner Trustee.

If (a) the Owner Trustee becomes a debtor subject to the reorganization provisions of the Bankruptcy Code, or any successor provision, (b) pursuant to such reorganization provisions the Owner Trustee is required, by reason of the Owner Trustee being held to have recourse liability directly or indirectly to the Holder of any Note or the Indenture Trustee, to make payment on account of any amount payable as principal or interest on such Note and (c) such Holder or the Indenture Trustee actually receives any Excess Amount (as hereinafter defined) which reflects any payment by the Owner Trustee on account of clause (b) of this Section, then such Holder or the Indenture Trustee, as the case may be, shall promptly refund to the Owner Trustee such Excess Amount. For purposes of this Section, "Excess Amount" means the amount by which such payment exceeds the amount which would have been received on or prior to the date of such payment by such Holder or the Indenture Trustee if the Owner Trustee had not become subject to the recourse liability referred to in clause (b) of this Section. Nothing contained in this Section shall prevent such Holder or the Indenture Trustee from enforcing any recourse obligation (and retaining the proceeds thereof) of the Owner Trustee expressly provided for under this Indenture.

SECTION 11.11. Bankruptcy of the Equity Participant.

The Indenture Trustee and the Holders of the Notes shall be bound by the provisions of Section 19(f) of the Participation Agreement.

SECTION 11.12. Counterpart Execution.

This Indenture and any amendment or supplement to this Indenture may be executed in any number of counterparts and by the different parties hereto and thereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument.

SECTION 11.13. Dating of Indenture.

Although this Indenture is dated for convenience and for the purpose of reference as of the date mentioned, the actual date or dates of execution by the Owner Trustee and the Indenture Trustee are as indicated by their respective acknowledgments hereto annexed.

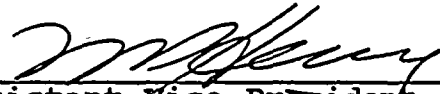
SECTION 11.14. Applicability of Annex A.

Notwithstanding any provision of this Indenture to the contrary, at all times that any Initial Series Notes are Outstanding, the terms and provisions of Annex A hereto shall supercede any contrary or inconsistent provision of this Indenture.

IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Indenture to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Security Pacific
Capital Leasing Corporation

By


Assistant Vice President

CHEMICAL BANK,

By


Vice President

IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Indenture to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Security Pacific
Capital Leasing Corporation

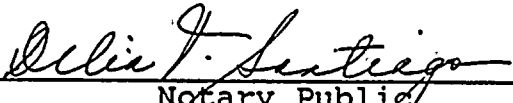
By _____
Assistant Vice President

CHEMICAL BANK,

By  _____
Vice President

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 17th day of August, 1986, before me personally came Martin P. Henry, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Scituate, Massachusetts; that he is an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, described in and which executed the foregoing instrument; that he knows the seal of said association; that the seal affixed to said instrument is such seal; that it was so affixed by authority of the by-laws of said association; and that he signed his name thereto on behalf of said association by like order.



Notary Public

[NOTARIAL SEAL]

Term Expires:

DELIA T. SANTIAGO
Notary Public, State of New York
No. 41-045186
Qualified in Queens County
Commission Expires March 30, 1987

STATE OF NEW YORK)
)
COUNTY OF NEW YORK) ss.:

On the 17th day of August, 1986, before me personally came JOHN J. FLEMING, to me known, who, being by me duly sworn, did acknowledged, depose and say that he resides at Brooklyn, New York; that he is Vice President of CHEMICAL BANK, a New York banking corporation, described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such seal; that it was so affixed by authority of the board of directors of said corporation; and that he signed his name thereto on behalf of said corporation by like order.

Anna Marie Napoli
Notary Public

[NOTARIAL SEAL]

Term Expires:

ANNA MARIE NAPOLI
Notary Public, State of New York -
No. 24-4759288
Qualified in Kings County
Certificate Filed in New York County
Commission Expires August 31, 1988

EXHIBIT A

FORM OF INITIAL SERIES NOTE

The Initial Series Note shall be substantially in the following form, with such omissions, insertions and variations as the Owner Trustee may determine with the approval of the Indenture Trustee and are not inconsistent with the provisions of the Indenture or as may be provided for in the Indenture:

THIS NOTE HAS NOT BEEN REGISTERED
UNDER THE SECURITIES ACT OF 1933 AND
MAY NOT BE TRANSFERRED, SOLD OR OFFERED
FOR SALE IN VIOLATION OF SUCH ACT.

NONRECOURSE PROMISSORY NOTE, INITIAL SERIES

No. _____ August __, 19 __
\$ _____

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity but solely as Owner Trustee ("Owner Trustee") under a Trust Agreement dated as of August 1, 1986 with _____ as Equity Participant, hereby promises to pay to _____ ("Lender"), or registered assigns, the principal sum of _____ DOLLARS (\$ _____) (the "Loan"), such payment to be made in semiannual installments on June 30 and December 30 of each year beginning December 30, 1986, and ending December 30, 2015, each installment to be in an amount equal to the original principal amount of this Initial Series Note ("Note") multiplied by the percentage set forth opposite the applicable date on Schedule 1 attached hereto, provided that the remaining unpaid principal amount of this Note, together with all accrued but unpaid interest, shall in any and all cases, be due and payable on December 30, 2015; and to pay interest on such principal amount from time to time outstanding hereunder at the rates, and in the manner and at the times specified below. Principal, interest and all other sums payable hereunder are payable in lawful money of the United States of America ("Dollars") no later than 10:00 a.m. (Los Angeles time) on the day when due in funds immediately available to Bank of America National Trust and Savings Association ("Bank of America") acting in its capacity as agent for Lender ("Agent") at Bank of America Corporate Service Center North, Department 1233, 1850 Gateway Boulevard, Concord, California 94520, Attention: Ms. Julie Hopkins (re: Arizona Public Service Company), or at such other place as Agent shall designate, for the account of Lender. As between Owner Trustee and Lender, payments to Agent constitute payments to Lender.

This Note is one of the Notes referred to in, and is entitled to the collateral and other benefits of, the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986 as amended or

supplemented in accordance with the provisions thereof (the "Indenture"), among Owner Trustee and Chemical Bank as Indenture Trustee, which Indenture provides for the acceleration of the maturity hereof upon the happening of certain stated events and for the obligation and the right of Owner Trustee to prepay the principal prior to the maturity hereof, in each case upon the terms and conditions therein and herein specified. Capitalized terms used in this Note which are not otherwise defined herein shall have the meanings ascribed to them in the Indenture.

1. Interest

Interest on the Loan shall be payable at the Variable Rate, provided, however, that during the period commencing on the date of this Note and ending on December 30, 1986 ("Option Period"), Owner Trustee may select in accordance with Paragraph 10 below, an interest rate applicable to the Loan equal to the Adjusted Eurodollar Rate. Notwithstanding the foregoing or any other provision of this Note, (i) the entire outstanding principal balance of this Note shall at all times be either a single Variable Rate Loan (as defined below) or a single Eurodollar Loan (as defined below), and (ii) Adjusted Eurodollar Rate shall not be applicable after December 30, 1986.

(a) "Variable Rate" shall mean the Applicable Percentage (as defined below) of the rate publicly announced from time to time by Bank of America in San Francisco, California, as its Reference Rate. Such rate is set by Bank of America based upon various factors, including Bank of America's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans; loans may be priced at, above or below the Reference Rate. Any change in the Variable Rate shall take effect on the day specified in the public announcement of such change; provided that in no event shall any such change take effect prior to the date of such announcement. While bearing interest at the Variable Rate, the Loan shall be referred to herein as the "Variable Rate Loan." "Applicable Percentage" shall equal (i) 100% for the period commencing on the date of this Note and ending December 31, 1986, (ii) 125% for the period commencing January 1, 1987, and ending May 31, 1987, (iii) 150% for the period commencing June 1, 1987, and ending August 31, 1987, and (iv) 200% thereafter.

(b) "Adjusted Eurodollar Rate" shall mean with respect to any Interest Period (as defined below), the percentage rate of interest per annum equal to 1.50 percent above the Eurodollar Rate. While bearing interest at the Adjusted Eurodollar Rate, the Loan shall be referred to

herein as a "Eurodollar Loan." "Eurodollar Rate" shall mean the per annum rate of interest determined by Agent to be the arithmetic mean, expressed as a percentage (rounded upwards, if necessary, to the nearest 1/100 of 1%), of the rates of interest per annum quoted to the Agent by each of Bank of America, Mellon Bank, and Chemical Bank (each a "Reference Bank" and collectively "Reference Banks") as the rate of interest per annum, net of reserves referred to in subparagraph (c) of Paragraph 3 below, at which Dollar deposits for such Interest Period and in the approximate aggregate amount of the Eurodollar Loans being maintained by such Reference Bank on the first day of such Interest Period under this Note and the Other Notes (as defined below) would be offered by such Reference Bank to major banks in the London inter-bank market upon request of such banks at approximately 11:00 a.m. (London time) three (3) Business Days before the commencement of such Interest Period. If any one of the Reference Banks shall be unable or shall otherwise fail to notify a rate, the mean rate shall be determined on the basis of the rate or rates notified by the other Reference Banks. "Other Notes" shall mean all other Initial Series Notes issued pursuant to the Indenture.

(c) "Interest Period" shall mean the period commencing on the date designated as the effective date of such Interest Period by Owner Trustee by notice to Agent in accordance with Paragraph 10 and ending on the numerically corresponding day of the next succeeding calendar month or, if there is no such numerically corresponding day, on the last day of such next succeeding calendar month; provided, however, that:

(i) if any Interest Period would end on a day that is not a Business Day, such Interest Period shall be extended to the next succeeding Business Day unless, such next succeeding Business Day would fall in the next calendar month, in which case such Interest Period shall end on the next preceding Business Day; and

(ii) the duration of any Interest Period which would otherwise end after the last day of the Option Period shall end on such last day.

2. Payment of Interest

Interest on the Loan shall accrue from the date made until paid in full at the applicable rate in effect from time to time and shall be payable as follows (a) as to the Variable Rate Loan, interest shall be payable monthly, in arrears, on the 30th day of such month, and (b) as to the Eurodollar Loan, interest shall be payable on the last day of each Interest Period with respect thereto; provided,

however, that interest shall accrue and be payable to the extent permitted by applicable law, on any amount that shall be overdue at a rate per annum equal to 2% over the interest rate then otherwise applicable under this Note, payable on demand by Agent.

3. Prepayment

(a) Premium. Upon at least five (5) Business Days' notice to Agent and provided that all the Other Notes shall concurrently be prepaid in whole in accordance with their respective terms, the outstanding principal amount of this Note may be prepaid but only in whole and not in part, and together with all accrued interest to the date of such prepayment, and together with any amount payable under subparagraph (c) of paragraph 8 below, and any premium in an amount calculated as a percentage of the original stated principal amount as follows: (i) .096% for the period from the date of this note through August 26, 1986, (ii) .072% for the period August 27, 1986 through September 2, 1986, (iii) .043% for the period September 3, 1986 through September 9, 1986, (iv) .024% for the period September 10, 1986 through September 16, 1986, and (v) none thereafter.

(b) Mandatory Prepayment. The unpaid principal balance outstanding under this Note shall be due and payable in full, together with interest accrued to the date of such payment, and premium, if any, calculated in accordance with subparagraph (a) above, and all other amounts due hereunder upon the occurrence of any of the following:

(i) Section 3.5 of the Indenture to the contrary notwithstanding, on the date of the issuance of any Additional Notes; or

(ii) upon the occurrence of any Indenture Event of Default, but only as provided in the Indenture.

4. Application of Payments

The Holder, by its acceptance of this Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. Holder further agrees, by its acceptance hereof, to duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Note unless and until all such notations have been duly made; provided, that neither the failure to make any such notation nor the inaccuracy of any such notation shall operate, or be deemed, to modify or impair any obligation of Owner Trustee hereunder.

5. Computations

All computations hereunder of interest on the Loan at the Adjusted Eurodollar Rate shall be based on a 360-day year and actual days elapsed, including the first day but excluding the last day; interest at the Variable Rate shall be computed on the basis of a year of 365 or 366 days, as the case may be.

6. Lending Offices

The Loan shall be made and maintained at any office designated by Lender from time to time for such purposes ("Lending Office"); provided, however, that the location of any such Lending Office shall not affect the obligation of Owner Trustee to repay the Loan at the Agent's office as provided above.

7. Payment on Non-Business Day

Subject to clause (i) of subparagraph (c) of Paragraph 1 above, whenever any payment to be made hereunder is stated to be due on a day that is not a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall be included in the computation of payment of interest.

8. Change in Circumstances Affecting Eurodollar Loans, Reserve Requirements, etc.

(a) Inability to Determine Eurodollar Rate. If at any time during the Option Period, Agent shall determine (which determination shall be made in good faith and shall be conclusive and binding upon Owner Trustee) that (i) by reason of circumstances then affecting the London interbank market, adequate and reasonable means do not or will not exist for ascertaining the interest rate applicable to a Eurodollar Loan, or (ii) Dollar deposits in the relevant amounts and for the relevant Interest Period are not available to the Lender in the London inter-bank market, then Agent shall forthwith give notice of such determination to the Owner Trustee at least one Business Day prior to the first day of any Interest Period so affected, whereupon, until Agent shall notify Owner Trustee that the circumstances giving rise to such suspension no longer exist (which notice shall be promptly given by Agent on discovery of such non-existence), (i) if the Variable Rate Loan is then outstanding, the obligations of the Lender to convert the Loan to a Eurodollar Loan shall be suspended and (ii) if the Eurodollar Loan is then outstanding, such Eurodollar Loan shall, automatically, on the last day of the then

current Interest Period therefor convert into a Variable Rate Loan.

(b) Illegality. If, after the date hereof, the introduction of or any change in any applicable law, rule or regulation or in the interpretation or administration thereof by any governmental authority charged with the interpretation or administration thereof or compliance by Lender with any request or directive (whether or not having the force of law) of any such authority shall make it unlawful or impractical for Lender (or its Lending Office) to make, maintain or fund its Eurodollar Loan, Lender shall forthwith give notice thereof to Agent and Owner Trustee. Before giving any notice pursuant to this subparagraph (b), Lender shall designate a different Lending Office if such designation will avoid the need for giving such notice and will not be otherwise disadvantageous to Lender in the sole judgment of Lender. Upon receipt of such notice (i) any pending conversion of the Loan into a Eurodollar Loan shall be withdrawn and the Loan shall continue instead as a Variable Rate Loan; and (ii) any outstanding Eurodollar Loan shall be automatically converted to a Variable Rate Loan, without premium or penalty, upon (x) the last day of the then current Interest Period if Lender may lawfully continue to fund and maintain such Eurodollar Loan to such day or (y) immediately if Lender may not lawfully continue to fund and maintain such affected Eurodollar Loan to such day.

(c) Reserve Requirements. Without limiting the effect of subparagraph (d) of this Paragraph 8, upon notice by Lender to Owner Trustee, Owner Trustee shall pay to Lender on the last day of each Interest Period for a Eurodollar Loan so long as Lender may be required to maintain reserves against "Eurocurrency liabilities" under (and as defined in) Regulation D of the Board of Governors of the Federal Reserve System (the "Board"), as additional interest on the unpaid principal amount of such Eurodollar Loan, an additional amount equal to such amount as would, together with payments of interest on such Eurodollar Loan for such Interest Period, result in the receipt by Lender of total interest on such Eurodollar Loan for such Interest Period at a rate equal to the rate determined in accordance with the following formula:

Adjusted Eurodollar Rate, divided by one
(1) minus the rate (expressed as a decimal) of such reserves then required by such Regulation D.

In determining the additional amount payable pursuant to this subparagraph (c) for any Interest Period, Lender shall (i) calculate the effect of reserve requirements in respect of Eurocurrency liabilities on its Eurodollar Loan as though

it had funded such Loan in the offshore Dollar market (whether or not so funded), without an offset or credit for such advances as Lender may make or may have made to its offshore branches or affiliates and (ii) take into account any transitional adjustment or phase-in provisions of such reserve requirements, applicable during such Interest Period, which would reduce the reserve requirement otherwise applicable to Eurocurrency liabilities during such Interest Period. Each such determination made by Lender, and each such notification by Lender to Owner Trustee under this subparagraph (c), shall be conclusive as to the matters therein as set forth in the absence of manifest error.

(d) Increased Cost. If any present or future applicable law, rule or regulation or any change therein or in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof or compliance by Lender (or its Lending Office) with any request or directive of any such authority, central bank or comparable agency, whether or not having the force of law:

(i) shall subject Lender (or its Lending Office) to any tax, duty or other charge with respect to the Eurodollar Loan or its obligation to make a Eurodollar Loan, or shall change the basis of taxation of payments to such Lender (or its Lending Office) of the principal of or interest with respect to its Eurodollar Loan, or in respect of any other amounts due under this Note in respect of its Eurodollar Loan, or its obligation to make a Eurodollar Loan (except for changes in the rate of tax on the overall net income of Lender or its Lending Office imposed by the jurisdiction in which such Lender's principal executive office or Lending Office is located); or

(ii) shall impose, modify or deem applicable any reserve (including, without limitation, any imposed by the Board), special deposit, compulsory loan or similar requirement against assets of, or deposits or other liabilities with, of or for the account of, or credit extended by, or shall impose on Lender (or its Lending Office), the London inter-bank market any other condition, affecting Lender's Eurodollar Loan, or its obligation to convert to a Eurodollar Loan;

and the result of any of the foregoing would in the opinion of Lender increase the cost to Lender (or its Lending Office) of making or maintaining its Eurodollar Loan, or reduce the amount of any sum received or receivable by

Lender (or its Lending Office) under this Note by an amount deemed by Lender to be material, then, within fifteen (15) days after written demand by Lender delivered to Owner Trustee by Agent, Owner Trustee will pay such additional amount or amounts as would compensate such Lender for increased cost or reduction. Lender will designate a different Lending Office if such designation will avoid the need for, or reduce the amount of, such compensation and will not be otherwise disadvantageous to Lender in the sole discretion of Lender. A certificate of Lender setting forth such additional amount or amounts necessary to compensate the Lender shall be conclusive in the absence of manifest error.

(e) Funding Indemnification. If, during the Option Period, Owner Trustee makes any payment of principal with respect to the Eurodollar Loan on a day other than the last day of the then current Interest Period, Owner Trustee shall reimburse Lender on demand for any loss incurred by it as a result of the timing of such payment not reflected in the Eurodollar Rate, including without limitation any loss incurred in liquidating or employing deposits from third parties and loss of profit for the period after such payment. A certificate of Lender setting forth the amounts necessary so as to reimburse it in respect of any loss shall be conclusive and binding absent manifest error.

(f) Funding of Eurodollar Loans. Lender is entitled to fund its Eurodollar Loan in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though Lender had actually funded the Eurodollar Loan through the purchase of offshore Dollar deposits in the London inter-bank market in the relevant amount and in maturities corresponding to the relevant Interest Period.

9. Taxes, Set-Off and Counterclaims with Respect to Eurodollar Loan.

Owner Trustee will pay to Agent for the account of Lender all amounts of principal, interest, premium and other fees and all other amounts due hereunder without set-off or counterclaim and free and clear of, and without deduction or withholding for or on account of, any present or future taxes, levies, imports, duties, assessments, restrictions, conditions or other charges of whatever nature, and all interest, penalties or similar liabilities with respect thereto, now or hereafter imposed, levied, collected, withheld or assessed by any country or by any political subdivision or taxing authority thereof or therein, on or with regard to the Eurodollar Loan contemplated in or by this Note, excluding income and franchise taxes of the

United States of America, or any political subdivision or taxing authority thereof or therein, and of the country in which Lender's Lending Office is located or any political subdivision or taxing authority thereof or therein.

In the event Owner Trustee is prohibited by operation of law from (i) making payments without deduction as provided hereinabove, or (ii) paying, causing to be paid, or reimbursing Lender for the cost of, any and all taxes, fees or other charges as provided hereinabove, then payments due to Lender under this Note shall be increased to such amount which, after provision for such taxes, fees or other charges, is necessary to yield and remit to Lender payments at the applicable rate specified in this Note.

Owner Trustee will furnish to Lender and Agent certified copies of tax receipts evidencing the payment of the amounts so levied or imposed within 90 days after the date any such payment is due pursuant to applicable law, unless any Lender shall have paid such tax or levy directly and received a receipt therefor.

10. Notices of Interest Rate Selection;
Failure to Provide Notice

Article III of the Indenture to the contrary notwithstanding, notices by Owner Trustee to Agent of prepayment of the Loan and of the conversion of the Loan from a Variable Rate Loan to a Eurodollar Loan or of the continuation of the Eurodollar Loan through the next succeeding Interest Period (together, in the case of each such conversion or continuation, with notice of the applicable Interest Period) shall be in writing (or by telephone promptly confirmed in writing) and shall be irrevocable and shall be effective only if received by Agent not later than 10:00 a.m. (Los Angeles time) ten (10) Business Days (in case of prepayment) and four (4) Business Days (in case of conversion or continuation) prior to the date of the relevant prepayment or the commencement of the applicable Interest Period, as the case may be; provided, however, that if Agent does not timely receive such notice of conversion to, or continuation of, the Eurodollar Loan, the Loan shall continue as, or convert (as of the last day of the current Interest Period) to, a Variable Rate Loan. Each such notice of prepayment, continuation or conversion shall specify (i) for any such prepayment or conversion, the date thereof, and (ii) for any such continuation or conversion, the duration of the applicable Interest Period.

11. Certain Miscellaneous Provisions

All payments, including payments of principal, premiums, if any, interest, and other sums to be made by Owner Trustee hereunder or under the Indenture shall be made only from the Lease Indenture Estate; and the Holder hereof, by its acceptance of this Note, agrees that such Holder will look solely to the Lease Indenture Estate and that Owner Trustee except as otherwise expressly provided in the Indenture is not personally liable to the Holder hereof for any amounts payable under this Note or the Indenture or any other Transaction Document; provided, however, that nothing in this paragraph shall be deemed or construed to limit or impair any right of the Indenture Trustee to declare an Indenture Event of Default, to accelerate the maturity of this Note, to declare the unpaid principal balance hereof to be due and payable in full, or otherwise to exercise any and all rights and remedies available under the Indenture, all as and to the extent provided in the Indenture.

This Note shall be construed and enforced in accordance with and governed by the law of New York applicable to contracts made and to be performed entirely within such State.

IN WITNESS WHEREOF, the Owner Trustee has caused this Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with _____.

By: _____

Title: _____

This Note is one of the
series of Notes referred to
therein and in the within-
mentioned Indenture.

CHEMICAL BANK
as Indenture Trustee,

By: _____
Authorized Officer

Schedule 1

Amortization of Initial Series Note

Amounts Stated as a percent of Original Principal

Original Principal Amount as a percent of Facility Cost : 80.0000000X

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
12/30/1986	2.9333333	2.9333333	0.0000000	100.0000000	8.00%
6/30/1987	5.2541784	5.0750000	0.1791784	99.8208216	10.15%
12/30/1987	5.2541784	5.0659067	0.1882717	99.6325500	10.15%
6/30/1988	5.2541784	5.0563519	0.1978265	99.4347235	10.15%
12/30/1988	5.2541784	5.0463122	0.2078661	99.2268574	10.15%
6/30/1989	5.2541784	5.0357630	0.2184154	99.0084420	10.15%
12/30/1989	5.2541784	5.0246784	0.2294999	98.7789421	10.15%
6/30/1990	5.2541784	5.0130313	0.2411471	98.5377950	10.15%
12/30/1990	5.2541784	5.0007931	0.2533853	98.2844097	10.15%
6/30/1991	5.2541784	4.9879338	0.2662446	98.0181652	10.15%
12/30/1991	5.2541784	4.9744219	0.2797565	97.7384087	10.15%
6/30/1992	5.2541784	4.9602242	0.2939541	97.4444546	10.15%
12/30/1992	5.2541784	4.9453061	0.3088723	97.1355823	10.15%
6/30/1993	5.2541784	4.9296308	0.3245476	96.8110347	10.15%
12/30/1993	5.2541784	4.9131600	0.3410184	96.4700163	10.15%
6/30/1994	5.2541784	4.8958533	0.3583250	96.1116913	10.15%
12/30/1994	5.2541784	4.8776683	0.3765100	95.7351813	10.15%
6/30/1995	5.2541784	4.8585604	0.3956179	95.3395633	10.15%
12/30/1995	5.2541784	4.8384828	0.4156955	94.9238678	10.15%
6/30/1996	5.2541784	4.8173863	0.4367921	94.4870757	10.15%
12/30/1996	5.2541784	4.7952191	0.4589593	94.0281165	10.15%
6/30/1997	5.2541784	4.7719269	0.4822515	93.5458650	10.15%
12/30/1997	6.4217736	4.7474526	1.6743209	91.8715441	10.15%
6/30/1998	6.4217736	4.6624809	1.7592927	90.1122514	10.15%
12/30/1998	6.4217736	4.5731968	1.8485768	88.2636746	10.15%
6/30/1999	6.4217736	4.4793815	1.9423921	86.3212825	10.15%
12/30/1999	6.4217736	4.3808051	2.0409685	84.2803140	10.15%
6/30/2000	6.4217736	4.2772259	2.1445476	82.1357664	10.15%
12/30/2000	6.4217736	4.1683901	2.2533834	79.8823830	10.15%
6/30/2001	6.4217736	4.0540309	2.3677426	77.5146404	10.15%
12/30/2001	6.4217736	3.9338680	2.4879056	75.0267348	10.15%
6/30/2002	6.4217736	3.8076068	2.6141667	72.4125681	10.15%
12/30/2002	6.4217736	3.6749378	2.7468357	69.6657323	10.15%
6/30/2003	6.4217736	3.5355359	2.8862376	66.7794947	10.15%
12/30/2003	6.4217736	3.3890594	3.0327142	63.7467805	10.15%
6/30/2004	6.4217736	3.2351491	3.1866245	60.5601560	10.15%
12/30/2004	6.4217736	3.0734279	3.3483456	57.2118104	10.15%
6/30/2005	6.4217736	2.9034994	3.5182742	53.6935362	10.15%
12/30/2005	6.4217736	2.7249470	3.6968266	49.9967096	10.15%
6/30/2006	6.4217736	2.5373330	3.8844405	46.1122691	10.15%
12/30/2006	6.4217736	2.3401977	4.0815759	42.0306932	10.15%
6/30/2007	6.4217736	2.1330577	4.2887159	37.7419773	10.15%
12/30/2007	6.4217736	1.9154053	4.5063682	33.2356091	10.15%
6/30/2008	6.4217736	1.6867072	4.7350664	28.5005427	10.15%
12/30/2008	6.4217736	1.4464025	4.9753710	23.5251716	10.15%

Schedule 1 - con't.

Amortization of Initial Series Note

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
6/30/2009	6.4217736	1.1939025	5.2278711	18.2973005	10.15%
12/30/2009	6.4217736	0.9285880	5.4931855	12.8041150	10.15%
6/30/2010	6.4217736	0.6498088	5.7719647	7.0321503	10.15%
12/30/2010	6.4217736	0.3568816	6.0648920	0.9672583	10.15%
6/30/2011	1.0163467	0.0490884	0.9672583	0.0000000	10.15%
12/30/2011	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2012	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2012	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2013	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2013	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2014	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2014	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%

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EXHIBIT B

ASSUMPTION AGREEMENT

TO: The Holders (as defined below) from time to time of the Notes (as defined below) of The First National Bank of Boston, not in its individual capacity, but solely as owner trustee under a Trust Agreement dated as of August 1, 1986 with Citizens Resources Company (in such capacity, the "Issuer") under the Trust Indenture, Mortgage, Security Agreement, and Assignment of Facility Lease (the "Indenture") dated as of August 1, 1986 between the Issuer and Chemical Bank, as trustee (the "Trustee").

The undersigned, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Obligor"), for the purpose of satisfying in part its obligation to make certain payments in respect of that certain Facility Lease dated as of August 1, 1986 between the Issuer and the Obligor (the "Facility Lease"), does hereby covenant and agree with the Holders (as defined in the Indenture) from time to time of the Notes (as defined in the Indenture) as follows:

SECTION 1. The Obligor does hereby agree to, and does hereby, assume unconditionally the payment of the principal of the Notes and of the interest and premium (if any) thereon, at the rates provided in the Notes, when and as the same shall become due and payable, whether at maturity or upon mandatory prepayment or upon declaration or otherwise, according to the terms of the Notes and of the Indenture. If any Initial Series Notes (as defined in the Indenture) are Outstanding (as defined in the Indenture), the Obligor agrees, upon surrender of the same to the Obligor for exchange at the Indenture Trustee's Office (as defined in the Indenture), together with the written request of the Holder of such Initial Series Note, or its attorney duly authorized in writing, in each case with signatures guaranteed, to exchange such Initial Series Note for a Bank Exchange Note in the same aggregate principal amount.

SECTION 2. The assumption herein contained shall be binding upon the Obligor, its successors and assigns, and shall remain in full force and effect irrespective of the power or authority of the Issuer to issue the Notes or to execute, acknowledge and deliver the Indenture or the validity of the Notes, or the Indenture, or of any defense whatsoever that the Issuer may or might have to the payment of the Notes (principal, interest or premium), or to the performance or observance of any of the provisions or conditions of the Indenture or any Note, or of the existence or continuance of the Issuer as a legal entity; nor shall said assumption be affected by the merger, consolidation, or other dissolution of the Issuer or the sale or other transfer of the property of the Issuer as an entirety, or substantially so, to any other person; nor shall the assumption be discharged or impaired by any act, failure or omission whatsoever on the part of any Holder of any Notes or the Trustee, including, among other such acts, failures and omissions, the following:

(a) any failure to present any Note for payment or to demand payment thereof, or to give to the Obligor notice of dishonor and non-payment of any Note when and as the same may become due and payable, or notice of any failure on the part of the Issuer to do any act or thing or to perform or keep any covenant or agreement by it to be done, kept or performed under the terms of Notes or the Indenture;

(b) any extension of the obligation of any Note, either indefinitely or for any period of time, or any other modification in the obligations under any Note or the Indenture or of the Issuer thereon or in connection therewith;

(c) any act or failure to act with regard to any Note or the Indenture or anything which might vary the risk of the Obligor; and

(d) any action taken under the Indenture and the Notes in the exercise of any right or power thereby conferred or any failure or omission on the part of the Trustee or the Holder of any Note to enforce any right or security given under the Indenture or any Note, or any waiver of any right or any failure or omission on the part of the Trustee or any Holder of any Note to enforce any right of any Holder of any Note against the Issuer;

provided, always, that the specific enumeration of the above mentioned acts, failures, waivers or omissions shall not be deemed to exclude any other acts, failures, waivers or omissions though not specifically mentioned herein, it being the purpose and intent of this Assumption Agreement that the obligation of the Obligor shall be absolute and unconditional to the extent herein specified and shall not be discharged, impaired or varied except by the payment of the principal of and interest on any Note and any premium thereon in case of prepayment, and then only to the extent of such payments.

SECTION 3. (a) Subject to the requirements of Section 10(b)(3)(ii) and the first sentence of Section 10(b)(3)(i) of the Participation Agreement and to the provisions of paragraph (b) of this Section, nothing contained in this Assumption Agreement shall prevent any consolidation or merger of the Obligor with or into any other corporation or corporations (whether or not affiliated with the Obligor), or successive consolidations or mergers in which the Obligor or its successor or successors shall be a party or parties, or shall prevent any sale, conveyance or lease of all or substantially all the property of the Obligor, to any other corporation authorized to acquire and operate the same; provided, however, and the Obligor hereby covenants and agrees, that upon any such consolidation, merger, sale, conveyance or lease, all obligations of the Obligor under this Assumption Agreement on or in respect of any Note, and the due and punctual performance and observance of all of the covenants and conditions of this Assumption Agreement to be performed by the Obligor, shall be expressly and duly assumed, by an agreement reasonably satisfactory in form and substance to the Trustee, executed and delivered by the corporation (if other than the Obligor) formed by such consolidation, or into which the Obligor shall have been merged, or by the corporation which shall have acquired such property.

(b) The Trustee, subject to applicable provisions of the Indenture, may rely upon an opinion of counsel to the Obligor as conclusive evidence that any such merger, consolidation, sale or conveyance complies with the provisions of this Section.

SECTION 4. The Obligor does hereby consent to all of the terms and conditions of each series of Notes and of the Indenture, and hereby waives any and all rights of notice of any fact or facts or circumstance or circumstances whatsoever and consents to any extension or extensions of time of any payment or payments, or of any other act or thing which any Holder or Holders of any Note or the Issuer may agree to consent to, either expressly, by acquiescence or otherwise, and hereby agrees not to claim or enforce any rights of subrogation or any other right or privilege which might otherwise arise on account of any payment made by it or act or thing done by it on account of or in accordance with its assumption herein contained, unless and until all of the Notes have been fully paid and discharged.

SECTION 5. The assumption herein expressed may be transferred or assigned at any time or from time to time and shall be considered to be transferred and assigned upon the transfer of any Note, whether with or without the consent of or notice to the Obligor or the Issuer. The Obligor hereby agrees to execute and deliver such instruments and to do such acts and things requested by the Trustee as shall be reasonably necessary to carry out and effectuate the purposes and intents of this Assumption Agreement. This Assumption Agreement may not be amended or modified in any respect without the prior written consent (evidenced as provided in the Indenture) of the Holders of not less than a majority in principal amount of the Notes Outstanding (as defined in the Indenture); provided, however, that without the written consent of the Holders of all of the Notes Outstanding, no such amendment or modification shall be effective which will change any of the provi-

sions of Sections 1, 2, 4 or 5 of this Assumption Agreement. The Obligor agrees to file with the Indenture Trustee a duplicate original of each such consent.

ARIZONA PUBLIC SERVICE COMPANY

By _____
Title:

ATTEST:

Title:

EXHIBIT C
FORM OF BANK EXCHANGE NOTE

ASSUMPTION AGREEMENT,
ALLONGE
AND NOVATION
OF
PROMISSORY NOTE

Date: _____

The undersigned ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Company"), in consideration of the release of the Company's obligations under that certain Facility Lease (the "Facility Lease"), dated as of August 1, 1986, between the Company as Lessee and The First National Bank of Boston, not in its individual capacity, but solely as owner trustee under a Trust Agreement dated as of August 1, 1986, with _____ (in such capacity, the "Issuer") as Lessor, hereby agrees personally, unconditionally and irrevocably to assume the outstanding obligations of the Issuer under the certain Note of the Issuer, issued by Issuer under that certain Trust Indenture, Mortgage, Security Agreement, and Assignment of Facility Lease dated as of August 1, 1986, between the Issuer and Chemical Bank, as trustee (the "Indenture"), to which Note this Assumption Agreement, Allonge and Novation of Promissory Note is affixed (the "Existing Note"); and, in order to induce the Holder (as such term is defined in the Indenture; all other capitalized terms used herein and not defined in Section 7 below or otherwise herein shall have the same respective meanings as defined in the Indenture) to consent to such release of the Company's obligations under the Facility Lease, which constitute part of the Lease Indenture Estate securing the Existing Note under the Indenture and to accept such assumption and the substitution of the Company for Issuer as obligor under the Existing Note, the Company hereby agrees to amend and modify the terms of the Existing Note, as set forth below. From and after the date of this Assumption Agreement, Allonge and Novation of Promissory Note, the terms and conditions set forth below (this "Note") shall amend and be substituted in their entirety for the terms of the Existing Note, and the obligations of the Company and the terms and conditions of this Note shall be as set forth herein, without reference to the Existing Note for any purpose.

THIS NOTE HAS NOT BEEN REGISTERED
UNDER THE SECURITIES ACT OF 1933 AND
MAY NOT BE TRANSFERRED, SOLD OR OFFERED
FOR SALE IN VIOLATION OF SUCH ACT.

RECOURSE PROMISSORY NOTE, INITIAL SERIES

No. _____

\$ _____

FOR VALUE RECEIVED, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Company"), hereby promises to pay to _____ ("Lender"), or registered assigns, the principal sum of dollars (\$ _____) (a "Loan"), such payment to be made in semiannual installments on June 30 and December 30 of each year beginning December 30, 1986, and ending December 30, 2015, each installment to be in an amount equal to the original principal amount of this Note multiplied by the percentage set forth opposite the applicable date on Schedule 1 attached hereto, provided that the remaining unpaid principal amount of this Note, together with all accrued but unpaid interest, shall in any and all cases, be due and payable on December 30, 2015; and to pay interest on such principal amount from time to time outstanding hereunder at the rates, and in the manner and at the times specified below. Both principal and interest are payable in lawful money of the United States of America ("Dollars") no later than 10:00 a.m. (Los Angeles time) on the day when due in funds immediately available to Bank of America National Trust and Savings Association ("Bank of America") acting in its capacity as agent for Lender ("Agent") at Bank of America Corporate Service Center-North, Department 1233, 1850 Gateway Boulevard, Concord, California 94520, Attention: Ms. Julie Hopkins (Re: Arizona Public Service Company), or at such other place as Agent shall designate, for the account of Lender. As between the Company and Lender, payments to Agent constitute payments to Lender.

This Note is one of the Notes referred to in, and is entitled to the collateral and other benefits of, the Indenture.

1. Interest Rate and Payment

Interest on the Loan shall be payable at a variable rate, per annum equal to two hundred percent (200%) of

* [As in original Note.]

** [As in original Note or, if applicable, the then current registered assign of such entity.]

the Reference Rate in effect from time to time as set forth below. "Reference Rate" shall mean the rate publicly announced from time to time by Bank of America in San Francisco, California, as its Reference Rate. Such rate is set by Bank of America based upon various factors, including Bank of America's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans; loans may be priced at, above, or below such Reference Rate. Any change in the Reference Rate shall take effect on the day specified in the public announcement of such change.

Interest on the Loan shall accrue from the date made until paid in full at the applicable rate in effect from time to time and shall be payable monthly, in arrears, on the first Business Day of each month.

2. Computations and Payment

All computations hereunder of interest on the Loan shall be computed on the basis of a year of 365 or 366 days, as the case may be. Whenever any payment to be made hereunder is stated to be due on a day that is not a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall be included in the computation of payment of interest. Funds received by the Agent after 10:00 a.m. (Los Angeles time) shall be deemed to have been received on the next succeeding Business Day.

3. Representations and Warranties

As an inducement to the Lender to accept this Note as aforesaid, the Company represents and warrants to the Lender as follows:

(a) Due Organization, Qualification, Etc. The Company is a corporation validly formed and existing and in good standing under the laws of the State of Arizona and is authorized to do business in the jurisdictions in which its ownership of property or conduct of business legally requires such authorization, and has full power, authority and legal right to own its properties and assets and to conduct its business as presently conducted or proposed to be conducted.

(b) Capacity. The Company has full power, authority and legal right to execute and deliver, and to perform and observe the provisions of this Note and has obtained all approvals and consents and completed all proceedings necessary to carry out the transactions contemplated hereby.

(c) Authority and Enforceability. The execution, delivery and performance by the Company of this Note and any

other instrument executed pursuant hereto, have been duly authorized by all necessary corporate action, and do not and will not require any approval of, notice to, or any action by, any Person (other than a Governmental Authority) and cannot and will not conflict with, result in any violation of, or constitute a default under, any provision of the articles of incorporation or bylaws of the Company or any agreement or other instrument binding upon or applicable to it, or any present law or governmental regulation or court decree or order applicable to it. This Note constitutes legal, valid and binding obligations of the Company enforceable against the Company in accordance with its terms, subject, as to enforcement only, to bankruptcy, insolvency, reorganization, moratorium or similar laws at the time in effect affecting the enforceability of the rights of creditors generally and to general principles of equity.

(d) Compliance with Other Instruments. The execution, delivery, and issuance of, and compliance with this Note will not result in a breach of any of the terms or conditions of, or result, except as contemplated by the Indenture, in the imposition of any lien, charge or encumbrance upon any properties of the Company pursuant to, or constitute a default (with due notice or lapse of time or both) or result in an occurrence of an event for which any holder or holders of Indebtedness may declare the same due and payable under, any indenture, agreement, order, judgment or instrument under which the Company is a party or by which the Company or its property may be bound or affected, or under its articles of incorporation or by-laws, and will not violate any provision of Applicable Law.

(e) Approvals. No authorization, registration with, consent or approval or other action by, and no notice to or filing with, any Governmental Authority or regulatory body is required for the due execution, delivery or performance by the Company of this Note, except for any such authorizations and approvals which have been duly obtained or made and are in full force and effect.

(f) Financial Information. The consolidated financial statements of the Company contained in the Company's Annual Report on Form 10-K for its latest full fiscal year (the "Form 10-K Report"), and in the Company's Form 10-Q Report for its latest full fiscal quarter (the "Form 10-Q Report"), filed with the Securities and Exchange Commission (the "SEC"), fairly present the consolidated financial position of the Company as at the dates indicated and the consolidated results of operations and sources of funds invested in utility plant and other plant for the periods therein specified, all in accordance with generally accepted accounting principles consistently applied, subject, in the case of the consolidated financial statements contained in the Form 10-Q Report, to the consolidation of

certain financial information and the omission of certain footnote disclosures, as permitted by the rules and regulations of the SEC, and to year-end audit adjustments. The Company represents and warrants that it knows of no such adjustments which would, if made on the date hereof, be material. Since the date of the Form 10-Q Report, and the Form 10-K Report, there has been no material adverse change in such consolidated financial position or operations.

(g) Litigation, Etc. Except as disclosed in the Form 10-K Report and the Form 10-Q Report, there are no actions, suits or proceedings (whether or not purportedly on behalf of the Company) pending, or to the knowledge of the Company threatened, against or affecting the Company, at law or in equity, before or by any Person, which, if adversely determined, would have a material adverse effect on the business, properties or the condition (financial or otherwise) of the Company. To the best of the Company's knowledge, (i) it is not in violation or default with respect to any applicable laws and/or regulations which materially affect the operations and/or condition (financial or otherwise) of the Company, (ii) it is not in violation or default with respect to any order, writ, injunction, demand or decree of any court or any Person the effect of which would be to materially affect the operations and/or conditions (financial or otherwise) of the Company, or (iii) it is not in violation or default (nor is there any waiver in effect which, if not in effect, would result in a violation or default) in any material respect under any agreement or instrument evidencing Debt, indenture, agreement or other instrument under which the Company is a party or may be bound, the effect of which would be to materially affect the operations and/or conditions (financial or otherwise) of the Company.

(h) Security Interests. The Lien of the Indenture constitutes a valid first priority perfected Lien upon and assignment and pledge of the property described therein as security for the payment and performance of the Company's obligations under and with respect to this Note, subject to no prior security or interest, claim, or right.

(i) No Default. To the best of the Company's knowledge, no Event of Default, nor any event which, with the lapse of time or the giving of notice, or both, would constitute an Event of Default, has occurred and is continuing.

(j) Title to the Undivided Interest; Security Interest. As of the date of this Assumption Agreement, Allonge and Novation to Promissory Note, the Company has good and marketable title to the Undivided Interest, including the related Generation Entitlement Share, free and clear of all Liens, except Permitted Liens, and to the Retained

Assets. All filings and recordings necessary or advisable to perfect and continue the Lien of the Indenture on the Lease Indenture Estate and to establish and maintain the continuing first priority of such Lien have been duly made.

4. Affirmative Covenants

Until payment in full of this Note, the Company agrees that:

(a) Fixed Charge Ratio. Maintain at all times a Fixed Charge Ratio of at least 2 to 1. "Fixed Charge Ratio" shall mean at any time the ratio of (A) the sum of (x) the consolidated net income of the Company and its subsidiaries for the twelve month period ending with the last month for which the Company has prepared a consolidated income statement, which period shall in no event end earlier than the last day of the month two months prior to the time of the calculation of the Fixed Charge Ratio (the "Twelve Month Period") plus (y) all income taxes deducted in determining said consolidated net income plus (z) the sum of (i) all interest expense in respect of Indebtedness deducted in determining said consolidated net income, (ii) all interest expense in respect of Funded Indebtedness being incurred at the time of the calculation of the Fixed Charge Ratio that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate and (iii) all interest expense in respect of Indebtedness other than Funded Indebtedness (I) incurred at any time subsequent to the Twelve Month Period and outstanding at the time of the calculation of the Fixed Charge Ratio and (II) being incurred at the time of the calculation of the Fixed Charge Ratio, that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate (the aggregate interest expense described in this clause (z) being referred to as the "Interest Expense") to (B) Interest Expense for such period.

(b) Financial Information. The Company will furnish to the Agent: (i) as soon as possible, and in any event within ten days after the Company knows or has reason to know of the occurrence of each Event of Default or each event which, with the giving of notice or lapse of time, or both, would constitute an Event of Default, continuing on the date of such statement, a statement of the chief financial officer (or in his absence, a principal financial officer) of the Company setting forth details of such Event of Default or event and the action which the Company proposes to take with respect thereto; (ii) as soon as possible, and in any event within fifteen days after filing each of the Company's Reports on Form 8-K with the Securities and Exchange Commission, a copy of each of such reports; (iii) as soon as available and in any event within

30 days after filing of each of the Company's Reports on Form 10-Q with the Securities and Exchange Commission, a copy of each of such reports together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Event of Default, or event which, with notice or lapse of time or both, would constitute an Event of Default, has occurred and is continuing or, if an Event of Default or such event has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereof and (y) setting forth, and certifying to the accuracy of, a current calculation of the Fixed Charge Ratio required under Section 4(a) hereof; (iv) as soon as available and in any event within 30 days after filing of each of the Company's Annual Reports on Form 10-K with the Securities and Exchange Commission, a copy of each of such reports, together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Event of Default, or event which, with notice or lapse of time or both, would constitute an Event of Default, has occurred and is continuing or, if an Event of Default or such event has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth, and certifying to the accuracy of, a current calculation of the Fixed Charge Ratio required under Section 4(a) hereof; and (vii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the Company as the Agent may from time to time reasonably request in writing.

(c) Insurance. The Company shall maintain insurance with responsible and reputable insurance entities or associations or through its own program of self insurance in such amounts and covering such risks as is usually carried by entities engaged in similar businesses and owning similar properties in the same general areas in which the Company operates.

(d) Other Debt. The Company will promptly pay and discharge any and all Indebtedness, liens, charges, all taxes, assessments and governmental charges or levies imposed upon it or upon its income or profits, or upon any of its properties prior to the date on which penalties accrue thereon, and lawful claims which, if unpaid, might become a lien or charge upon the property of the Company, the effect of which would materially affect the operations and/or conditions (financial or otherwise) of the Company, except such as may in good faith be contested or disputed, or for which arrangements for deferred payment have been made, provided appropriate reserves are maintained to the reasonable satisfaction of the Agent.

(e) Maintenance of Existence. The Company will cause to be done at all times all things necessary to maintain the corporate existence of the Company.

(f) Conduct of Business. The Company will do or cause to be done all things necessary to preserve and keep in full force and effect its material franchises; provided, however, that the Company may discontinue or permit the discontinuance of any material franchise if (x) its board of directors shall determine that such discontinuance is necessary or desirable in the conduct of its business and does not materially and adversely affect or diminish any right of the Lender hereunder or (y) the Company continues to provide electric service to the area covered by such material franchise to the substantially same extent and on substantially the same terms and conditions as provided prior to such discontinuance pending the renegotiation or renewal thereof.

(g) Expenses. The Company will pay all reasonable out-of-pocket expenses of the Agent (including, but not limited to, fees and disbursements of the Agent's independent and in-house counsel) incident to the administration of the obligations evidenced by this Note, including the fees and charges of Agent, any amendments or waivers to this Note, the protection of the rights of the Lender or Agent under this Note or the Indenture and the enforcement of payment of this Note, whether by judicial proceedings or otherwise. The obligations of the Company under this Section 4(g) shall survive payment and cancellation of this Note.

(h) Books and Records. The Company will at all times keep books of record and account reflecting its business affairs and transactions in which proper entries will be made of said business affairs and its transactions in accordance with generally accepted accounting principles.

(i) Inspection. At any reasonable time and from time to time, permit Lender or any agents or representatives thereof to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its subsidiaries with any of their respective officers or directors; provided, however, that the Company reserves the right to restrict access to any of its generating facilities in accordance with reasonably adopted procedures relating to safety and security; and provided, further, that, Subsection (g) above notwithstanding, the costs and expenses incurred by Lender or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions occurring or made prior to the occurrence of an Event of Default shall be for the account of Lender. Lender

agrees to use reasonable efforts to ensure that any information concerning the Company or any of its subsidiaries obtained by Lender pursuant to this Subsection which is not contained in a report or other document filed with the Securities and Exchange Commission, distributed by the Company to its shareholders or otherwise available to the public generally will, to the extent permitted by law and except as may be required by valid subpoena or in the normal course of Lender's business operations be treated confidentially by Lender and will not be distributed or otherwise made available by Lender to any person or entity, other than the Agent or the Lender's or the Agent's employees, authorized agents or representatives.

(j) Operation and Maintenance. The Company will operate and maintain Unit 2 in accordance with the terms and provisions of Section 8(a) of the Facility Lease, as such Section 8(a) was in effect immediately following the execution and delivery of the Facility Lease by the Company, and notwithstanding any subsequent amendment, expiration or termination of the Facility Lease. Such Section 8(a) is incorporated herein by reference.

(k) Maintenance of Equity. Maintain at all times common stock equity, as calculated in accordance with generally accepted accounting principles consistently applied and set forth from time to time in the consolidated balance sheets of the Company and its subsidiaries, of at least \$1.4 billion.

5. Events of Default

If one or more of the following described events shall occur ("Event of Default"):

(a) The Company shall fail to pay in full any principal hereof or interest hereon when the same becomes due; or

(b) The Company shall fail to perform or observe any of the provisions contained in any other Section of this Note and such failure shall continue for more than thirty (30) days after notice to the Company from the Agent or the Lender of such failure; or

(c) Any representation or warranty made in writing by or on behalf of the Company herein or pursuant hereto, or otherwise in connection with the transactions contemplated hereby or any report, certificate, financial or other instrument furnished in connection with this Note, shall prove to have been false or incorrect in any

material respect, or omits to state a material fact required to be stated therein in order to make the statements contained therein, in the light of the circumstances under which made, not misleading, on the date as of which made; or

(d) The Company shall cause a default as defined in any evidence of Indebtedness of the Company in aggregate principal amount in excess of \$20,000,000, or under any indenture, agreement or other instrument under which the same may be issued and, as a result thereof, the holder of such evidence of Indebtedness shall accelerate the maturity thereof; or

(e) The Company shall commence a voluntary case or other proceeding seeking liquidation, reorganization or other relief with respect to itself or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, or shall consent to any such relief or to the appointment of or taking of possession by any such official in an involuntary case or other proceeding commenced against it, or shall make a general assignment for the benefit of creditors, or shall take any corporate action to authorize any of the foregoing; or an involuntary case or other proceeding shall be commenced against the Company seeking liquidation, reorganization or other relief with respect to it or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, and such involuntary case or other proceeding shall remain undismissed or unstayed for a period of 60 days consecutive days; or

(f) final judgment for the payment of money in excess of \$5,000,000 shall be rendered against the Company and the Company shall not have discharged the same or provided for its discharge in accordance with its terms or bonded the same or procured a stay of execution thereof within 60 days from the entry thereof;

THEN, or at any time thereafter:

(1) Where the Company is in default under the provisions of Section 5(e), the entire unpaid principal

amount of this Note, all interest accrued and unpaid thereon and all other amounts payable hereunder shall automatically become and be forthwith due and payable, without presentment, demand, protest or notice of any kind, all of which are hereby expressly waived by the Company;

(2) In any other case referred to in this Section 5, the Holder may, at its option, by written notice to the Company, declare the entire unpaid principal amount of this Note, all interest accrued and unpaid thereon and all other amounts payable hereunder to be forthwith due and payable, whereupon the same shall become immediately due and payable, without presentment, demand, protest or further notice of any kind, all of which are hereby expressly waived by the Company.

In the case of either (1) or (2) above, the Holder may immediately and without expiration of any period of grace, enforce payment of all Obligations of the Company to it under this Note, and with the Agent and through the Indenture Trustee may exercise all available rights and remedies under the Indenture and Applicable Law.

6. Definitions

As used herein, and unless otherwise defined herein, the following terms shall have the following respective meanings:

"Funded Indebtedness" means the Indebtedness evidenced by this Note and all other Indebtedness which matures more than one year from the date of its creation or matures within one year from such date but is renewable or extendible, at the option of the Company, to a date more than one year from such date or arises under a revolving credit or similar agreement which obligates the lender or lenders to extend credit during a period of more than one year from such date including, without limitation, all amounts of Funded Indebtedness required to be paid or prepaid within one year from the date of its creation.

"Guaranteed Indebtedness" of any Person means all Indebtedness referred to in clause (i), (ii) or (iii) of the definition of "Indebtedness" in this Section guaranteed directly or indirectly in any manner by such Person, or in effect guaranteed directly or indirectly by such Person through an agreement (i) to pay or purchase such Indebtedness or to advance or supply funds for the payment or purchase of such Indebtedness, or (ii) to purchase, sell or lease (as lessee or lessor) property, or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such Indebtedness or to assure the holder of such Indebtedness against loss, or (iii) to supply funds to or in any other manner invest in the debtor (including

any agreement to pay for property or services irrespective of whether or not such property is received or such services are rendered), or (iv) otherwise to assure a creditor against loss.

"Imputed Rate" means, in respect of Indebtedness, the actual initial rate of interest per annum to be paid by a Person with respect to such Indebtedness.

"Indebtedness" of any Person means (i) all indebtedness of such person for borrowed money or for the deferred purchase price of property or services, (ii) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property acquired by such Person (even though the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property), (iii) all obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, recorded as capital leases in respect of which such Person is liable as lessee, (iv) all Guaranteed Indebtedness, and (v) all Indebtedness referred to in clause (i), (ii) or (iii) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any lien, security interest or other charge or encumbrance upon or in property (including, without limitation, accounts and contracts rights) owned by such Person, even though such person has not assumed or become liable for the payment of such Indebtedness.

"Obligations" shall mean and include all loans, advances, debits, liabilities, obligations, letters of credit or acceptance transactions, trust receipt transactions, or any other financial accommodations, howsoever arising, owing by the Company to, or on behalf of, the Lender of every kind and description (whether or not evidenced by any note or other instrument and whether or not for the payment of money), direct or indirect, absolute or contingent, due or to become due, now existing or hereafter arising pursuant to the terms of this Note, including, without limitation, all interest, fees, charges, expenses, attorneys' fees and accountants' fees chargeable to the Company or incurred by the Lender or Agent in connection with its dealings with the Company.

7. Miscellaneous

(a) No Waiver. No failure to exercise, and no delay in exercising any right, power or remedy hereunder or under any document delivered pursuant hereto shall impair any right, power or remedy which the Lender may have, nor shall any such delay be construed to be a waiver of any of such rights, powers or remedies, or an acquiescence in any

breach or default under this Note or any document delivered pursuant hereto, nor shall any waiver of any breach or default of the Company hereunder be deemed a waiver of any default or breach subsequently occurring. The rights and remedies herein specified are cumulative and not exclusive of any rights or remedies which the Lender or Agent would otherwise have.

(b) Notices. All notices, requests, consents and demands hereunder shall be in writing and shall be effective when duly deposited in the mails, registered mail postage prepaid, or delivered to the telegraph company or transmitted by telex, addressed to the respective party at the address set forth below, except that notices to the Lender or Agent pursuant to this Section 8(b) shall not be effective until received.

Company: Arizona Public Service Company
411 North Central Avenue
P.O. Box 53999
Phoenix, Arizona 85072-3999
Attn: Secretary

Holder or Agent: Bank of America National Trust
and Savings Association
555 S. Flower Street
Los Angeles, California 90071
Attn: Mr. Gregory House

With a copy to:

Bank of America National Trust
and Savings Association
Bank of America Corporate
Service Center - North
Department 1233
1850 Gateway Boulevard
Concord, California 94520
Attn: Ms. Julie Hopkins
(Re: Arizona Public Service
Company)

Any of the parties hereto may change their respective address by notice in writing given to the other parties to this Agreement.

(c) Termination. This Note shall terminate only when all Obligations of the Company incurred hereunder and evidenced hereby shall have been discharged in full.

(d) Severability of Provisions. In case any one or more of the provisions contained in this Note should be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining

provisions contained herein shall not in any way be affected or impaired thereby.

(e) Recourse Note. Notwithstanding anything to the contrary contained in the Existing Note as previously in effect prior to this Assumption Agreement, Allonge and Novation of Promissory Note and notwithstanding anything to the contrary contained in the Lease or in the Indenture or in any other agreement, the Company shall be personally liable to the Holder of this Note for any and all amounts payable under this Note or the Indenture.

IN WITNESS WHEREOF, the Company has caused this Assumption Agreement, Allonge and Novation of Promissory Note to be duly executed as of the day and year first above written.

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona Corporation

By: _____

Name: _____

Title: _____

This Note is one of the series of Notes referred to therein and in the within-mentioned Indenture.

CHEMICAL BANK
As Indenture Trustee,

By _____
Authorized Officer

Schedule 1 - Amortization of the
Bank Exchange Note

Original Principal Amount as a percent of Facility Cost : 80.0000000X

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
12/30/1986	2.9333333	2.9333333	0.0000000	100.0000000	8.00%
6/30/1987	5.2541784	5.0750000	0.1791784	99.8208216	10.15%
12/30/1987	5.2541784	5.0659067	0.1882717	99.6325500	10.15%
6/30/1988	5.2541784	5.0563519	0.1978265	99.4347235	10.15%
12/30/1988	5.2541784	5.0463122	0.2078661	99.2268574	10.15%
6/30/1989	5.2541784	5.0357630	0.2184154	99.0084420	10.15%
12/30/1989	5.2541784	5.0246784	0.2294999	98.7789421	10.15%
6/30/1990	5.2541784	5.0130313	0.2411471	98.5377950	10.15%
12/30/1990	5.2541784	5.0007931	0.2533853	98.2844097	10.15%
6/30/1991	5.2541784	4.9879338	0.2662446	98.0181652	10.15%
12/30/1991	5.2541784	4.9744219	0.2797565	97.7384087	10.15%
6/30/1992	5.2541784	4.9602242	0.2939541	97.4444546	10.15%
12/30/1992	5.2541784	4.9453061	0.3088723	97.1355823	10.15%
6/30/1993	5.2541784	4.9296308	0.3245476	96.8110347	10.15%
12/30/1993	5.2541784	4.9131600	0.3410184	96.4700163	10.15%
6/30/1994	5.2541784	4.8958533	0.3583250	96.1116913	10.15%
12/30/1994	5.2541784	4.8776683	0.3765100	95.7351813	10.15%
6/30/1995	5.2541784	4.8585604	0.3956179	95.3395633	10.15%
12/30/1995	5.2541784	4.8384828	0.4156955	94.9238678	10.15%
6/30/1996	5.2541784	4.8173863	0.4367921	94.4870757	10.15%
12/30/1996	5.2541784	4.7952191	0.4589593	94.0281165	10.15%
6/30/1997	5.2541784	4.7719269	0.4822515	93.5458650	10.15%
12/30/1997	6.4217736	4.7474526	1.6743209	91.8715441	10.15%
6/30/1998	6.4217736	4.6624809	1.7592927	90.1122514	10.15%
12/30/1998	6.4217736	4.5731968	1.8485768	88.2636746	10.15%
6/30/1999	6.4217736	4.4793815	1.9423921	86.3212825	10.15%
12/30/1999	6.4217736	4.3808051	2.0409685	84.2803140	10.15%
6/30/2000	6.4217736	4.2772259	2.1445476	82.1357664	10.15%
12/30/2000	6.4217736	4.1683901	2.2533834	79.8823830	10.15%
6/30/2001	6.4217736	4.0540309	2.3677426	77.5146404	10.15%
12/30/2001	6.4217736	3.9338680	2.4879056	75.0267348	10.15%
6/30/2002	6.4217736	3.8076068	2.6141667	72.4125681	10.15%
12/30/2002	6.4217736	3.6749378	2.7468357	69.6657323	10.15%
6/30/2003	6.4217736	3.5355359	2.8862376	66.7794947	10.15%
12/30/2003	6.4217736	3.3890594	3.0327142	63.7467805	10.15%
6/30/2004	6.4217736	3.2351491	3.1866245	60.5601560	10.15%
12/30/2004	6.4217736	3.0734279	3.3483456	57.2118104	10.15%
6/30/2005	6.4217736	2.9034994	3.5182742	53.6935362	10.15%
12/30/2005	6.4217736	2.7249470	3.6968266	49.9967096	10.15%
6/30/2006	6.4217736	2.5373330	3.8844405	46.1122691	10.15%
12/30/2006	6.4217736	2.3401977	4.0815759	42.0306932	10.15%
6/30/2007	6.4217736	2.1330577	4.2887159	37.7419773	10.15%
12/30/2007	6.4217736	1.9154053	4.5063682	33.2356091	10.15%
6/30/2008	6.4217736	1.6867072	4.7350664	28.5005427	10.15%
12/30/2008	6.4217736	1.4464025	4.9753710	23.5251716	10.15%

Schedule 1 - Amortization of the
Bank Exchange Note

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
6/30/2009	6.4217736	1.1939025	5.2278711	18.2973005	10.15%
12/30/2009	6.4217736	0.9285880	5.4931855	12.8041150	10.15%
6/30/2010	6.4217736	0.6498088	5.7719647	7.0321503	10.15%
12/30/2010	6.4217736	0.3568816	6.0648920	0.9672583	10.15%
6/30/2011	1.0163467	0.0490884	0.9672583	0.0000000	10.15%
12/30/2011	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2012	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2012	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2013	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2013	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2014	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2014	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
6/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%

LHC:NYPC-sp loan.wr1

1. The effectiveness of Section 6.11 of the Indenture is suspended in its entirety and the following provisions shall apply in lieu thereof:

Except as otherwise provided in this Section, but notwithstanding any contrary or inconsistent provision of the Indenture, subject, however, to Section 10.2 of the Indenture, (a) at all times prior to the occurrence of an Indenture Event of Default, the Owner Trustee shall retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree or consent to any amendment to, or any waiver, discharge or termination of, or give any consent under any term or provision of Sections 2(c), 3(g), 4, 7, 8(f) (iv), 9(i), 11, 15(i) (x), (i) (y), (vii) and (x) and the provisions relating to the redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease; and, provided, further, that the Owner Trustee shall, in any event, observe and perform its covenants contained in clause (iv) of Section 6.1 of the Indenture; and, provided, further, that during the continuance of any Event of Default the Owner Trustee shall promptly provide the Indenture Trustee with notice or copies of any notice, consent, waiver or approval given or received and any other action taken under clause (a); (b) upon and for a period not to exceed 60 days after the occurrence of an Indenture Event of Default described in clause (y) of paragraph (a) of Section 6.3 of the Indenture, (i) the Owner Trustee and the Agent shall consult and cooperate in good faith, and, the Owner Trustee and the Indenture Trustee shall act or refrain from acting concurrently, in exercising all rights, powers and remedies of each arising under the Facility Lease and the Indenture, respectively, in all

instances with a view to protecting and preserving the respective rights and remedies of the Owner Trustee and the Holders of the Notes under the Facility Lease and the Indenture and, to the extent reasonably practicable, maximizing the prospects of recovery; without limiting the generality of the foregoing, the Owner Trustee and Indenture Trustee shall jointly exercise all rights enumerated in clause (a) above; (c) upon and at all times after the occurrence of an Indenture Event of Default described in clause (x) (ii) of paragraph (a) of Section 6.3 of the Indenture or under the circumstances described in clause (x) (i) of such paragraph, the Indenture Trustee shall have, and may freely exercise, to the exclusion of the Owner Trustee, all rights enumerated in clause (a) above and under the Indenture; provided however, that nothing in this Section shall be deemed or construed to require the Owner Trustee or Indenture Trustee to act or refrain from acting in violation of Applicable Law, nor shall the exercise of any rights, powers and remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee as defined in the ANPP Participation Agreement. Notwithstanding any provision of this Section to the contrary (other than the proviso to the preceding sentence), the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the "Stated Price") and (iii) Owner Trustee shall not have notified the Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date within 60 days after the date of such notice of election. If the Owner Trustee shall fail timely to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate to any Person (other than the Indenture Trustee, Agent or any Holder(s) or Affiliates of any thereof) at a price no lower than the Stated Price at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the Stated Price, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all of the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate. At any time after the

termination of the Facility Lease or expiration of the 180 day period described in the second preceding sentence, the Indenture Trustee may exercise any right under Applicable Law to dispose of any interest in the Lease Indenture Estate, free of any right of the Owner Trustee to purchase the same.

2. Notwithstanding anything to the contrary contained in Section 6.8(c) of the Indenture, the Owner Trustee shall not terminate the Facility Lease or arrange for the substitution of another Person as lessee under a new lease without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

3. Notwithstanding anything to the contrary contained in Section 2.3 of the Indenture, there shall be no release of all or any portion of the Lease Indenture Estate from the security or other interest created by Section 2.1 of the Indenture without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

4. If at the time any Special Transfer is affected, the Lessee shall not have assumed the obligations under the Initial Series Notes, any subsequent breach by Lessee of its covenants contained in Section 10(b)(3)(vii) of the Participation Agreement shall be an event of Default and an Indenture Event of Default.

5. Any failure by the Owner Trustee to pay the Initial Series Notes in full when and as required by Section 13(d) or Section 14(b) or 14(c) shall be an Indenture Event of Default.

6. The provisions of this Annex A shall prevail to the extent they are inconsistent with or contrary to the provisions of any of the Transaction Documents.

7. The provisions of this Annex A shall remain in full force and effect until the full payment of all principal of and premium, if any, and interest on the Initial Series Notes.

ARIZONA PUBLIC SERVICE COMPANY

Sale and Leaseback of an Undivided
Interest in Palo Verde Nuclear Generating
Station Unit 2

Security Pacific Capital Leasing Corporation

TRANSACTION DOCUMENTS

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When Recorded, Return to: David A. Sprentall
SNELL & WILMER
3100 Valley Bank Center
Phoenix, Arizona 85073

SUPPLEMENTAL INDENTURE NO. 1

Dated as of November 1, 1986

To

TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF
FACILITY LEASE

Dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON, not in its indi-
vidual capacity, but solely as Owner Trustee under
a Trust Agreement dated as of August 1, 1986
with Security Pacific Capital Leasing
Corporation

and

CHEMICAL BANK,
as Indenture Trustee

Original Indenture Recorded on August 18, 1986, as Instrument
No. 86-439433 in Maricopa County, Arizona Recorder's Office.

SUPPLEMENTAL INDENTURE No. 1 dated as of November 1, 1986 to Trust Indenture, Mortgage, Security Agreement and Assignment Of Facility Lease dated as of August 1, 1986, between THE FIRST NATIONAL BANK OF BOSTON, a national banking association (FNB), not in its individual capacity, but solely as Owner Trustee (the Owner Trustee) under a Trust Agreement dated as of August 1, 1986, between FNB, whose address is 100 Federal Street, Boston, Massachusetts 02110, with Security Pacific Capital Leasing Corporation, a Delaware corporation, and CHEMICAL BANK, a New York banking corporation (the Indenture Trustee), whose address is 55 Water Street, New York, New York 10041.

W I T N E S S E T H:

WHEREAS, the Owner Trustee and the Indenture Trustee have entered into a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986 (the Indenture) pursuant to which the Owner Trustee has issued the Initial Series Notes;

WHEREAS, Section 3.5(1) of the Indenture provides, among other things, that the Initial Series Notes may be refunded with Refunding Notes;

WHEREAS, Section 3.5(4) of the Indenture provides, among other things, that the Owner Trustee and the Indenture Trustee may enter into indentures supplemental to the Indenture for, among other things, the purpose of establishing the terms, conditions and designations of Refunding Notes;

WHEREAS, the Owner Trustee desires to issue Refunding Notes to effect a refunding of the Initial Series Notes and to enter into this Supplemental Indenture No. 1 to establish the terms, conditions and designations of such Refunding Notes; and

WHEREAS, Section 10.1(viii) of the Indenture provides that, without the consent of Holders of the Notes Outstanding, the Indenture Trustee may, with the written consent of the Owner Trustee, from time to time and at any time execute a supplement to the Indenture in order to evidence the issuance of, and to provide the terms of, Refunding Notes;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein and not otherwise defined herein shall have the meanings assigned to such terms in Appendix A attached hereto.

SECTION 2. Terms, Conditions and Designations of the Refunding Notes.

(a) The Refunding Notes

There is hereby created and established a separate series of Notes of the Owner Trustee designated "Nonrecourse Promissory Notes, Refunding Series 1986", herein referred to as the Refunding Notes. The Refunding Notes shall be payable as to principal and bear interest on the principal amount thereof as follows:

<u>Refunding Note Due</u>	<u>Interest Rate</u>	<u>Original Principal Amount</u>
December 30, 1998	9.00%	\$ 14,228,000
June 30, 2015	10.45	98,772,000
		<u>\$113,000,000.00</u>

The Refunding Note due December 30, 1998 shall be substantially in the form of Exhibit A-1 to this Supplemental Indenture No. 1. The Refunding Note due June 30, 2015 shall be substantially in the form of Exhibit A-2 to this Supplemental Indenture No. 1. Each Refunding Note shall bear interest on the principal amount thereof from time to time Outstanding from the Issue Date designated thereon until paid at the rate of interest set forth therein, which interest shall be payable on December 30, 1986 and on each June 30 and December 30 thereafter to and including the maturity date thereof, unless paid in full prior to such date as provided herein and in such Refunding Note. The principal amount of each Refunding Note shall be payable on the dates and in the amounts as set forth in Schedule 1 attached thereto, as such Schedule may be adjusted from time to time in accordance with the terms hereof and of such Refunding Note. Installments of interest on and principal of (and premium, if any, on) each Refunding Note shall be due and payable on the payment dates specified in Schedule 1 attached thereto.

Each Refunding Note shall be subject to prepayment as set forth in such Refunding Note.

(b) Certain Adjustments to Amortization Schedules.

The schedule of principal amortization attached to each Refunding Note may be adjusted at the discretion of the Owner Trustee on one occasion prior to June 30, 1989; provided, however, that no such adjustment shall be made by the Owner Trustee which will increase or reduce the average life of such Refunding Note (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than six months; provided

further, however, such adjustment may be made only in connection with an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease. If the Owner Trustee shall elect to make the foregoing adjustment, the Owner Trustee shall deliver to the Indenture Trustee and to the Lessee at least 60 days prior to the first payment date (specified on the schedule to such Refunding Note) proposed to be affected by such adjustment, a certificate of the Owner Trustee (x) stating that the Owner Trustee has elected to make such adjustment, (y) setting forth the revised schedule of principal amortization for such Refunding Note and (z) attaching calculations showing that the average life of such Refunding Note will not be reduced or increased except as permitted by this paragraph (b). The Indenture Trustee may rely on such Owner Trustee certificate and shall have no duty with respect to the calculations referred to in the foregoing clause (z).

SECTION 3. Amendments to Indenture.

(a) The Table of Contents to the Indenture is amended hereby to delete the reference to Schedule I.

(b) The fourth and fifth WHEREAS clauses of the Indenture are amended hereby in their entirety to read as follows:

"WHEREAS, in the circumstances contemplated by Sections 2(d), 2(e) and 2(f) of the Participation Agreement, the Owner Trustee may desire to issue Refunding Notes (together with any other Notes issued hereunder other than the Initial Series Notes, the Additional Notes) or to increase the principal amount of the Outstanding Refunding Notes or to change the amortization of either or both thereof;

WHEREAS, in order to finance the Supplemental Financing Amount of Capital Improvements and to refund notes of any series previously issued, the Owner Trustee may desire to issue Additional Notes hereunder secured on a pari passu basis with other Notes Outstanding from time to time;"

(c) Section 2.3 of the Indenture is amended hereby by replacing the capitalized term "Lien" in the first sentence of Section 2.3 with the clause "security and other interests" and by replacing the phrase "opinion relates" in the first sentence of Section 2.3 with the phrase "opinion relate".

(d) Section 3.5(1) of the Indenture is amended hereby by inserting the term "Extraordinary Casualty Value," after the term "Casualty Value," in the first sentence of Section 3.5(1).

(e) Section 3.5(2) of the Indenture is amended hereby by replacing the clause "the date of issuance" in the first sentence of Section 3.5(2) with the clause "the proposed date of issuance".

(f) Section 3.5(4)(b)(iv) of the Indenture is amended hereby by inserting the term ", Extraordinary Casualty Value" after the term "Casualty Value" in Section 3.5(4)(b)(iv).

(g) Section 3.9(b) of the Indenture is amended hereby by inserting the clause "or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement" after the term "Cure Option" in the first sentence of Section 3.9(b).

(h) Section 3.9(c) of the Indenture is amended hereby by inserting the clause "or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement" before the period at the end of Section 3.9(c).

(i) Section 3.12 of the Indenture is amended hereby by inserting the following immediately after the first semicolon in Section 3.12:

"provided, however, that no such adjustment shall be made by the Owner Trustee which will increase or reduce the average life of such Refunding Notes (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than six months;"

and replacing the phrase "provided, however" in Section 3.12 with the phrase "provided further, however".

(j) Section 5.2 of the Indenture is amended hereby by amending the first and second sentence of Section 5.2 in their entirety as follows:

"If an Event of Loss or Deemed Loss Event shall occur or the Lessee shall exercise the Cure Option or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement, any amounts of Casualty Value, Special Casualty Value, Extraordinary Casualty Value or Fair Market Sales Value received or held by the Indenture Trustee in respect of such Event of Loss or Deemed Loss Event or exercise of the Cure Option or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement shall, except as otherwise provided in Section 5.3, be distributed forthwith to the Equity Participant. If the Lessee or Owner Trustee, as the case may be, shall exercise its option to terminate the Facility Lease pursuant to Section 14 thereof, then there shall be prepaid, on the Obsolescence Redemption Date, the unpaid

principal amount of all Notes and all accrued but unpaid interest thereon to the date of such prepayment, to the extent that there shall have been paid or provision made for payment of the amounts due on the Notes on the Obsolescence Redemption Date."

(k) Section 6.2(g) of the Indenture is amended hereby by replacing the reference "7(b)(i)" in Section 6.2(g) with the reference "7(b)(1)".

(l) Section 6.4(e) of the Indenture is amended hereby by replacing the term "ANPP Project Agreement" in Section 6.4(e) with the term "ANPP Project Agreements".

(m) Section 6.8(a) of the Indenture is amended hereby by replacing the clause "on the date such Basic Rent was payable" in Section 6.8(a) with the clause "on the date such Rent was payable".

(n) Section 10.2 of the Indenture is amended hereby by deleting the following in Section 10.2 in its entirety:

"Notwithstanding the foregoing, the Indenture Trustee shall, upon receipt of a written instruction from the Lessee and the Owner Trustee, consent to an amendment of any definitions contained in or appended to this Indenture which are being changed pursuant to the amendments, if any, referred to in Section 10(b)(3)(xii) of the Participation Agreement."

(o) Section 10.3 of the Indenture is amended hereby by replacing the term "the Facility Lease" in Section 10.3 with the term "any Granting Clause Document".

(p) Appendix A to the Indenture is hereby deleted and replaced by Appendix A attached hereto.

(q) Exhibit B to the Indenture is amended hereby by replacing the phrase "Citizens Resources Company" in the heading thereof with the phrase "Security Pacific Capital Leasing Corporation".

SECTION 4. Miscellaneous.

(a) Execution.

This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of

execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Execution as Supplemental Indenture.


This Supplemental Indenture No. 1 is executed and shall be construed as an indenture supplemental to the Indenture and, as provided in the Indenture, this Supplemental Indenture No. 1 forms a part thereof.

(c) Disclosure.

Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation. The address of the beneficiary is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.


IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Supplemental Indenture No. 1 to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Security Pacific
Capital Leasing Corporation

By 
Martin P. Henry
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK,
as Indenture Trustee

By 
T. J. Foley
Vice President

Date: November 19, 1986

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 19th day of November, 1986, before me personally came MARTIN P. HENRY, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Boston, Massachusetts; that he is Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, described in and which executed the foregoing instrument; and that he signed his name thereto on behalf of said association by authority of the Board of Directors of said corporation.

David A. Spivak
Notary Public

[NOTARIAL SEAL]

Term Expires:

DAVID A. SPIVAK
Notary Public, State of New York
No. 100140
Queens County
Commission Expires 12/31/87 7

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 19th day of November, 1986, before me personally came T. J. FOLEY, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Bethpage, New York; that he is a Vice President of CHEMICAL BANK, a New York banking corporation described in and which executed the foregoing instrument; and that he signed his name thereto on behalf of said corporation by authority of the Board of Directors of said corporation.

David A. Spivak

Notary Public

[NOTARIAL SEAL]

Term Expires:

DAVID A. SPIVAK
Notary Public, State of New York
No. 314687-83
Qualified County
Comm. 2097

EXHIBIT A-1
TO SUPPLEMENT NO. 1

FORM OF REFUNDING NOTE
(DUE DECEMBER 30, 1998)

THIS NOTE HAS NOT BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933 AND MAY NOT BE TRANSFERRED,
SOLD OR OFFERED FOR SALE IN VIOLATION OF SUCH ACT

NONRECOURSE PROMISSORY NOTE, REFUNDING SERIES 1986
(DUE DECEMBER 30, 1998)

Issued at: New York, New York

Issue Date: November 19, 1986

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (Owner Trustee) under a Trust Agreement dated as of August 1, 1986 with Security Pacific Capital Leasing Corporation (the Equity Participant), hereby promises to pay to PVNGS FUNDING CORP., INC., or registered assigns, the principal sum of Fourteen Million Two Hundred Twenty Eight Thousand Dollars (\$14,228,000), such payment to be made in the amounts and on the dates specified in Schedule 1 hereto, as such Schedule 1 may be revised in accordance herewith; and to pay interest (computed on the basis of a 360-day year of twelve 30-day months) on the aggregate amount of such principal sum remaining unpaid from time to time from the date of this Refunding Note until due and payable, semiannually in arrears on June 30 and December 30 in each year, commencing December 30, 1986, at the rate of 9.00% per annum, until the principal hereof is paid in full.

Capitalized terms used in this Refunding Note which are not otherwise defined herein shall have the meanings ascribed thereto in the Indenture (as hereinafter defined).

In the event any date on which a payment is due under this Refunding Note is not a Business Day, then payment thereof may be made on the next succeeding Business Day with the same force and effect as if made on the date on which such payment was due and no interest in respect of such payment shall accrue for the period from and after such due date.

All payments of principal, and premium, if any, and interest to be made by the Owner Trustee hereunder and under the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986, as at any time heretofore or

hereafter amended or supplemented in accordance with the provisions thereof (the Indenture), between the Owner Trustee and Chemical Bank, as Trustee (the Indenture Trustee), shall be made only from the Lease Indenture Estate and the Trust Estate and the Indenture Trustee shall have no obligation for the payment thereof except to the extent that the Indenture Trustee shall have sufficient income or proceeds from the Lease Indenture Estate to make such payments in accordance with the terms of Article V of the Indenture. The Holder hereof, by its acceptance of this Refunding Note, agrees that such Holder will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to the Holder hereof as above provided, and that neither the Equity Participant nor, except as expressly provided in the Indenture, the Owner Trustee nor the Indenture Trustee is or shall be personally liable to the Holder hereof for any amounts payable under this Refunding Note or for any performance to be rendered under the Indenture or any other Transaction Document or for any liability thereunder; provided, however, that in the event the Lessee shall assume all the obligations of the Owner Trustee hereunder and under the Indenture pursuant to Section 3.9(b) of the Indenture, then all the payments to be made under this Refunding Note shall be made only from payments made by the Lessee under this Refunding Note in accordance with the Assumption Agreement referred to in said Section 3.9(b) and the Holder of this Refunding Note agrees that in such event it will look solely to the Lessee for such payment and, subject to Section 2.4 of the Indenture, to the Lease Indenture Estate.

Principal, and premium, if any, and interest shall be payable in immediately available funds 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, in the manner provided in the Indenture, on presentment of this Refunding Note at the Indenture Trustee's Office, or as otherwise provided in the Indenture.

In the manner and to the extent provided in the Indenture, Schedule 1 hereto may be adjusted once at the discretion of the Owner Trustee prior to June 30, 1989, in connection with an adjustment to Basic Rent under Section 3(d) of the Facility Lease.

In the event of any partial prepayment of this Refunding Note (other than pursuant to the payment of principal in accordance with Schedule 1 hereto), the principal amount of this Refunding Note to be paid thereafter pursuant to Schedule 1 hereto shall be adjusted proportionately; provided that, all such adjustments shall be rounded to the nearest \$1000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of this Refunding Note which is prepaid. In connection with such adjustments the Owner Trustee shall deliver to the Indenture Trustee, not later than 60 days prior to the next date

on which a payment of principal of this Refunding Note is due following such partial prepayment, a revised Schedule 1 hereto. The Indenture Trustee may rely on such revised Schedule 1 and shall have no duty with respect to the adjustments set forth therein other than to make it available for inspection by the Holder of this Note.

The Holder hereof, by its acceptance of this Refunding Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. The Holder of this Refunding Note agrees, by its acceptance hereof, that it will duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Refunding Note unless and until all such notations have been duly made.

This Refunding Note is one of the Refunding Notes referred to in the Indenture. The Indenture permits the issuance of additional series of Notes, as provided in Section 3.5 of the Indenture, and the several series may be for varying aggregate principal amounts and may have different maturity dates, interest rates, redemption provisions and other terms. The properties of the Owner Trustee included in the Lease Indenture Estate are pledged to the Indenture Trustee to the extent provided in the Indenture as security for the payment of the principal of and premium, if any, and interest on this Refunding Note and all other Notes issued and outstanding from time to time under the Indenture. Reference is hereby made to the Indenture for a statement of the rights of the Holders of, and the nature and extent of the security for, this Refunding Note and of the rights of, and the nature and extent of the security for, the Holders of the other Notes and of certain rights of the Owner Trustee, as well as for a statement of the terms and conditions of the trust created by the Indenture, to all of which terms and conditions the Holder hereof agrees by its acceptance of this Refunding Note.

This Refunding Note is subject to purchase by the Owner Trustee as provided in Section 6.8(b) of the Indenture and to mandatory prepayment in full as provided in Section 5.2 of the Indenture, such prepayment being without premium but including accrued interest to the date of prepayment. In addition, this Refunding Note may be prepaid in whole or in part at any time on or after December 30, 1991 by the Owner Trustee as follows: upon the giving of not less than 30 days' notice as provided in the Indenture and at the following prepayment prices (expressed as a percentage of the unpaid principal amount hereof), together with interest accrued to the date fixed for prepayment:

If prepaid during the
twelve months beginning
December 30,

Prepayment
Price

1991	104.50%
1992	103.60%
1993	102.70%
1994	101.80%
1995	100.90%

and thereafter at the principal amount thereof, together with interest accrued to the date fixed for prepayment.

In case an Indenture Event of Default shall occur and be continuing, the unpaid balance of the principal of this Refunding Note and any other Notes, together with all accrued but unpaid interest thereon, may, subject to certain rights of the Owner Trustee and the Equity Participant contained or referred to in the Indenture, be declared or may become due and payable in the manner and with the effect provided in the Indenture.

The lien upon the Lease Indenture Estate is subject to being legally discharged prior to the maturity of this Refunding Note upon the deposit with the Indenture Trustee of cash or certain securities sufficient to pay this Refunding Note when due in accordance with the terms of the Indenture.

There shall be maintained at the Indenture Trustee's Office a register for the purpose of registering transfers and exchanges of Notes in the manner provided in the Indenture. The transfer of this Refunding Note is registrable, as provided in the Indenture, upon surrender of this Refunding Note for registration of transfer duly accompanied by a written instrument of transfer duly executed by or on behalf of the registered Holder hereof, together with the amount of any applicable transfer taxes. Prior to due presentment for registration of transfer of this Refunding Note, the Owner Trustee and the Indenture Trustee may treat the person in whose name this Refunding Note is registered as the owner hereof for the purpose of receiving payments of principal of and premium, if any, and interest on this Refunding Note and for all other purposes whatsoever, whether or not this Refunding Note be overdue, and neither the Owner Trustee nor the Indenture Trustee shall be affected by notice to the contrary.

This Refunding Note shall be governed by, and construed in accordance with, the law of the State of New York.

IN WITNESS WHEREOF, the Owner Trustee has caused this Refunding Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under a Trust Agreement
dated as of August 1, 1986 with
Security Pacific Capital
Leasing Corporation

By _____
Martin P. Henry
Assistant Vice President

This Note is one of the series of Notes referred to therein
and in the within-mentioned Indenture.

CHEMICAL BANK,
as Indenture Trustee

By _____
T. J. Foley
Vice President

SCHEDULE 1
TO THE REFUNDING NOTE
(DUE DECEMBER 30, 1998)

Schedule of Principal Amortization

<u>Payment Date</u>	<u>Principal Amount Payable</u>	<u>Principal Balance</u>
December 30, 1989	\$ 65,000	\$14,163,000
June 30, 1990	367,000	13,796,000
December 30, 1990	384,000	13,412,000
June 30, 1991	401,000	13,011,000
December 30, 1991	419,000	12,592,000
June 30, 1992	438,000	12,154,000
December 30, 1992	458,000	11,696,000
June 30, 1993	478,000	11,218,000
December 30, 1993	500,000	10,718,000
June 30, 1994	522,000	10,196,000
December 30, 1994	546,000	9,650,000
June 30, 1995	571,000	9,079,000
December 30, 1995	596,000	8,483,000
June 30, 1996	623,000	7,860,000
December 30, 1996	651,000	7,209,000
June 30, 1997	680,000	6,529,000
December 30, 1997	2,081,000	4,448,000
June 30, 1998	2,175,000	2,273,000
December 30, 1998	2,273,000	0

Principal Amount	<u>\$14,228,000</u>
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ASSIGNMENT

Date: November 19, 1986

For value received, PVNGS FUNDING CORP., INC. hereby sells, assigns and transfers to CHEMICAL BANK as Collateral Trust Trustee pursuant to the Collateral Trust Indenture dated as of November 1, 1986, as heretofore amended and supplemented, among PVNGS FUNDING CORP., INC., Arizona Public Service Company and said Collateral Trust Trustee, without recourse, the Refunding Note to which this Assignment is annexed and all rights thereunder.

PVNGS FUNDING CORP., INC.

By _____
Vice President

EXHIBIT A-2
TO SUPPLEMENT NO. 1

FORM OF REFUNDING NOTE
(DUE JUNE 30, 2015)

THIS NOTE HAS NOT BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933 AND MAY NOT BE TRANSFERRED,
SOLD OR OFFERED FOR SALE IN VIOLATION OF SUCH ACT

NONRECOURSE PROMISSORY NOTE, REFUNDING SERIES 1986
(DUE JUNE 30, 2015)

Issued at: New York, New York

Issue Date: November 19, 1986

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (Owner Trustee) under a Trust Agreement dated as of August 1, 1986 with Security Pacific Capital Leasing Corporation (the Equity Participant), hereby promises to pay to PVNGS FUNDING CORP., INC., or registered assigns, the principal sum of Ninety Eight Million Seven Hundred Seventy Two Thousand Dollars (\$98,772,000), such payment to be made in the amounts and on the dates specified in Schedule 1 hereto, as such Schedule 1 may be revised in accordance herewith; and to pay interest (computed on the basis of a 360-day year of twelve 30-day months) on the aggregate amount of such principal sum remaining unpaid from time to time from the date of this Refunding Note until due and payable, semiannually in arrears on June 30 and December 30 in each year, commencing December 30, 1986, at the rate of 10.45% per annum, until the principal hereof is paid in full.

Capitalized terms used in this Refunding Note which are not otherwise defined herein shall have the meanings ascribed thereto in the Indenture (as hereinafter defined).

In the event any date on which a payment is due under this Refunding Note is not a Business Day, then payment thereof may be made on the next succeeding Business Day with the same force and effect as if made on the date on which such payment was due and no interest in respect of such payment shall accrue for the period from and after such due date.

All payments of principal, and premium, if any, and interest to be made by the Owner Trustee hereunder and under the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986, as at any time heretofore or hereafter amended or supplemented in accordance with the provisions thereof (the Indenture), between the Owner Trustee and Chemical Bank,

as Trustee (the Indenture Trustee), shall be made only from the Lease Indenture Estate and the Trust Estate and the Indenture Trustee shall have no obligation for the payment thereof except to the extent that the Indenture Trustee shall have sufficient income or proceeds from the Lease Indenture Estate to make such payments in accordance with the terms of Article V of the Indenture. The Holder hereof, by its acceptance of this Refunding Note, agrees that such Holder will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to the Holder hereof as above provided, and that neither the Equity Participant nor, except as expressly provided in the Indenture, the Owner Trustee nor the Indenture Trustee is or shall be personally liable to the Holder hereof for any amounts payable under this Refunding Note or for any performance to be rendered under the Indenture or any other Transaction Document or for any liability thereunder; provided, however, that in the event the Lessee shall assume all the obligations of the Owner Trustee hereunder and under the Indenture pursuant to Section 3.9(b) of the Indenture, then all the payments to be made under this Refunding Note shall be made only from payments made by the Lessee under this Refunding Note in accordance with the Assumption Agreement referred to in said Section 3.9(b) and the Holder of this Refunding Note agrees that in such event it will look solely to the Lessee for such payment and, subject to Section 2.4 of the Indenture, to the Lease Indenture Estate.

Principal, and premium, if any, and interest shall be payable in immediately available funds 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, in the manner provided in the Indenture, on presentment of this Refunding Note at the Indenture Trustee's Office, or as otherwise provided in the Indenture.

In the manner and to the extent provided in the Indenture, Schedule 1 hereto may be adjusted once at the discretion of the Owner Trustee prior to June 30, 1989, in connection with an adjustment to Basic Rent under Section 3(d) of the Facility Lease.

In the event of any partial prepayment of this Refunding Note (other than pursuant to the payment of principal in accordance with Schedule 1 hereto), the principal amount of this Refunding Note to be paid thereafter pursuant to Schedule 1 hereto shall be adjusted proportionately; provided that, all such adjustments shall be rounded to the nearest \$1000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of this Refunding Note which is prepaid. In connection with such adjustments the Owner Trustee shall deliver to the Indenture Trustee, not later than 60 days prior to the next date on which a payment of principal of this Refunding Note is due following such partial prepayment, a revised Schedule 1 hereto. The

Indenture Trustee may rely on such revised Schedule 1 and shall have no duty with respect to the adjustments set forth therein other than to make it available for inspection by the Holder of this Note.

The Holder hereof, by its acceptance of this Refunding Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. The Holder of this Refunding Note agrees, by its acceptance hereof, that it will duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Refunding Note unless and until all such notations have been duly made.

This Refunding Note is one of the Refunding Notes referred to in the Indenture. The Indenture permits the issuance of additional series of Notes, as provided in Section 3.5 of the Indenture, and the several series may be for varying aggregate principal amounts and may have different maturity dates, interest rates, redemption provisions and other terms. The properties of the Owner Trustee included in the Lease Indenture Estate are pledged to the Indenture Trustee to the extent provided in the Indenture as security for the payment of the principal of and premium, if any, and interest on this Refunding Note and all other Notes issued and outstanding from time to time under the Indenture. Reference is hereby made to the Indenture for a statement of the rights of the Holders of, and the nature and extent of the security for, this Refunding Note and of the rights of, and the nature and extent of the security for, the Holders of the other Notes and of certain rights of the Owner Trustee, as well as for a statement of the terms and conditions of the trust created by the Indenture, to all of which terms and conditions the Holder hereof agrees by its acceptance of this Refunding Note.

This Refunding Note is subject to purchase by the Owner Trustee as provided in Section 6.8(b) of the Indenture and to mandatory prepayment in full as provided in Section 5.2 of the Indenture, such prepayment being without premium but including accrued interest to the date of prepayment. In addition, this Refunding Note may be prepaid in whole or in part at any time on or after December 30, 1991 by the Owner Trustee as follows: upon the giving of not less than 30 days' notice as provided in the Indenture and at the following prepayment prices (expressed as a percentage of the unpaid principal amount hereof), together with interest accrued to the date fixed for prepayment:

If prepaid during the
twelve months beginning
December 30,

Prepayment
Price

1991	107.70%
1992	107.15%
1993	106.60%
1994	106.05%
1995	105.50%
1996	104.95%
1997	104.40%
1998	103.85%
1999	103.30%
2000	102.75%
2001	102.20%
2002	101.65%
2003	101.10%
2004	100.55%

and thereafter at the principal amount thereof, together with interest accrued to the date fixed for prepayment.

In case an Indenture Event of Default shall occur and be continuing, the unpaid balance of the principal of this Refunding Note and any other Notes, together with all accrued but unpaid interest thereon, may, subject to certain rights of the Owner Trustee and the Equity Participant contained or referred to in the Indenture, be declared or may become due and payable in the manner and with the effect provided in the Indenture.

The lien upon the Lease Indenture Estate is subject to being legally discharged prior to the maturity of this Refunding Note upon the deposit with the Indenture Trustee of cash or certain securities sufficient to pay this Refunding Note when due in accordance with the terms of the Indenture.

There shall be maintained at the Indenture Trustee's Office a register for the purpose of registering transfers and exchanges of Notes in the manner provided in the Indenture: The transfer of this Refunding Note is registrable, as provided in the Indenture, upon surrender of this Refunding Note for registration of transfer duly accompanied by a written instrument of transfer duly executed by or on behalf of the registered Holder hereof, together with the amount of any applicable transfer taxes. Prior to due presentment for registration of transfer of this Refunding Note, the Owner Trustee and the Indenture Trustee may treat the person in whose name this Refunding Note is registered as the owner hereof for the purpose of

receiving payments of principal of and premium, if any, and interest on this Refunding Note and for all other purposes whatsoever, whether or not this Refunding Note be overdue, and neither the Owner Trustee nor the Indenture Trustee shall be affected by notice to the contrary.

This Refunding Note shall be governed by, and construed in accordance with, the law of the State of New York.

IN WITNESS WHEREOF, the Owner Trustee has caused this Refunding Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under a Trust Agreement
dated as of August 1, 1986 with
Security Pacific Capital
Leasing Corporation

By _____
Martin P. Henry
Assistant Vice President

This Note is one of the series of Notes referred to therein and in the within-mentioned Indenture.

CHEMICAL BANK,
as Indenture Trustee

By _____
T. J. Foley
Vice President

SCHEDULE 1
TO THE REFUNDING NOTE
(DUE JUNE 30, 2015)

Schedule of Principal Amortization

<u>Payment Date</u>	<u>Principal Amount Payable</u>	<u>Principal Balance</u>
June 30, 1999	\$2,375,000	\$96,397,000
December 30, 1999	2,499,000	93,898,000
June 30, 2000	2,630,000	91,268,000
December 30, 2000	2,767,000	88,501,000
June 30, 2001	2,431,000	86,070,000
December 30, 2001	2,011,000	84,059,000
June 30, 2002	2,073,000	81,986,000
December 30, 2002	2,138,000	79,848,000
June 30, 2003	2,205,000	77,643,000
December 30, 2003	2,274,000	75,369,000
June 30, 2004	2,208,000	73,161,000
December 30, 2004	2,277,000	70,884,000
June 30, 2005	2,300,000	68,584,000
December 30, 2005	2,372,000	66,212,000
June 30, 2006	2,446,000	63,766,000
December 30, 2006	2,522,000	61,244,000
June 30, 2007	2,601,000	58,643,000
December 30, 2007	2,682,000	55,961,000
June 30, 2008	2,766,000	53,195,000
December 30, 2008	2,852,000	50,343,000
June 30, 2009	2,941,000	47,402,000
December 30, 2009	3,033,000	44,369,000
June 30, 2010	3,128,000	41,241,000
December 30, 2010	3,225,000	38,016,000
June 30, 2011	3,326,000	34,690,000
December 30, 2011	3,430,000	31,260,000
June 30, 2012	3,537,000	27,723,000
December 30, 2012	3,647,000	24,076,000
June 30, 2013	5,000,000	19,076,000
December 30, 2013	4,528,000	14,548,000
June 30, 2014	6,776,000	7,772,000
December 30, 2014	7,130,000	642,000
June 30, 2015	642,000	0

Principal Amount \$98,772,000

ASSIGNMENT

Date: November 19, 1986

For value received, PVNGS FUNDING CORP., INC. hereby sells, assigns and transfers to CHEMICAL BANK as Collateral Trust Trustee pursuant to the Collateral Trust Indenture dated as of November 1, 1986, as heretofore amended and supplemented, among PVNGS FUNDING CORP., INC., Arizona Public Service Company and said Collateral Trust Trustee, without recourse, the Refunding Note to which this Assignment is annexed and all rights thereunder.

PVNGS FUNDING CORP., INC.

By _____
Vice President

ASSIGNMENT, ASSUMPTION

AND

FURTHER AGREEMENT

dated as of August 1, 1986

between

ARIZONA PUBLIC SERVICE COMPANY,

and

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity, but
solely as Owner Trustee under a Trust
Agreement with Security Pacific
Capital Leasing Corporation

Sale and Leaseback of an Undivided Interest
in Palo Verde Nuclear Generating Station Unit 2

THIS ASSIGNMENT, ASSUMPTION AND FURTHER AGREEMENT, dated as of August 1, 1986, between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), and THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (the Owner Trustee), under a Trust Agreement, dated as of August 1, 1986, with SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation, as Equity Participant (the Equity Participant).

W I T N E S S E T H :

WHEREAS, APS and the other ANPP Participants are parties to the ANPP Participation Agreement (such terms and all other terms used in these recitals without definition having the respective definitions to which reference is made in Article I below); and

WHEREAS, APS has sold, and the Owner Trustee has purchased, the Undivided Interest and the Real Property Interest for and in consideration of the payment to APS by the Owner Trustee of the Purchase Price, the purchase price of the Real Property Interest and the assignments and assumptions herein set forth;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

For purposes hereof, unless otherwise defined herein, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A hereto. References in this Agreement to articles, sections and clauses are to articles, sections and clause in this Agreement unless otherwise indicated.

ARTICLE II

NONPARTITIONMENT

SECTION 2.01. Nonpartitionment. The Owner Trustee hereby waives any rights it may have to partition Unit 2, whether by partitionment in kind or by sale and division of proceeds, and further agrees that it will not resort to any action in law or in equity to partition Unit 2, and it waives the benefits of all laws that may now or hereafter authorize such partition for a term (i) which shall be coterminous with the ANPP Participation Agreement or (ii) which shall be for such lesser period as may be required under Applicable Law.

ARTICLE III

ASSIGNMENTS; EXERCISE OF RIGHTS

SECTION 3.01. Assignment of Warranties. The Lessee hereby ASSIGNS to the Owner Trustee an undivided interest, equal to the Unit 2 Interest in, to and under all of APS's rights under any and all warranties of and other claims against dealers, manufacturers, vendors, contractors and subcontractors relating to Unit 2.

SECTION 3.02. Assignment of the ANPP Participation Agreement. (a) The Lessee hereby ASSIGNS to the Owner Trustee an undivided interest, equal to the Unit 2 Interest in, to and under all of APS's rights under the ANPP Participation Agreement, to the extent that such rights relate to the Undivided Interest (including, but without limitation, a percentage entitlement equal to the Unit 2 Interest of the Net Energy Generation and Available Generating Capability (as each such term is defined in the ANPP Participation Agreement) of Unit 2).

(b) The Owner Trustee hereby ASSIGNS to the Lessee the rights assigned under paragraph (a) until the Lease Termination Date.

SECTION 3.03. Exercise of Rights as Participant under the ANPP Participation Agreement. (a) Except as provided in Sections 15.2.2, 15.6.4 and 15.10 of the ANPP Participation Agreement (or any comparable successor provision) APS shall be and remain the sole "Participant" for all purposes of the ANPP

Participation Agreement and the sole representative (with power to bind) in all dealings with the other ANPP Participants in relation to the Undivided Interest, the Real Property Interest and the rights assigned to the Owner Trustee pursuant to this Agreement; provided, however, that the foregoing shall not limit in any way any liability or obligation that APS may incur to the Owner Trustee or the Equity Participant under any Transaction Document as a result thereof.

(b) Unless the ANPP Participation Agreement shall otherwise permit, any right conferred on the Owner Trustee by Section 15.2.2 of the ANPP Participation Agreement shall be exercised as required by Section 15.6.3.3 of said Agreement.

(c) The provisions of this Section 3.03 shall remain in full force and effect until such time as the ANPP Administrative Committee or the ANPP Participants shall otherwise consent by amendment to the ANPP Participation Agreement or otherwise.

ARTICLE IV

ASSUMPTION; RELEASE

SECTION 4.01. Assumption by Owner Trustee. Except as contemplated by Section 5(a) of the Facility Lease, the Owner Trustee agrees that, effective on and as of the Lease Termination Date (unless a Transferee (Transferee) shall have qualified under Section 15.10 of the ANPP Participation Agreement or any comparable successor provision), unless a Default or Event of Default shall have occurred and be continuing or an Event of Loss shall have occurred or a Deemed Loss Event shall have been declared, the Owner Trustee shall assume and agree to pay, perform and discharge the Unit 2 Interest of all liabilities and obligations of APS under, or with respect to, the ANPP Project Agreements, attributable to Unit 2, other than any and all costs relating to, allocable to, or incurred in connection with, Decommissioning.

SECTION 4.02. Release. Upon the assumption and agreement by a Transferee pursuant to Section 4.01 (whether at the Lease Termination Date or thereafter), the Owner Trustee shall therewith and thereupon be released and discharged from its obligations under

Section 4.01 arising on or after such assumption and agreement.

ARTICLE V

NO RELEASE OF APS; REIMBURSEMENT

SECTION 5.01. No Release of APS. Notwithstanding the provisions of Article IV or any other provision hereof or of any other Transaction Document, and except to the extent provided in Section 15.10 of the ANPP Participation Agreement (or any comparable successor provision), APS shall not be released from any liability or obligation under the ANPP Project Agreements, or otherwise, with respect to PVNGS, and APS shall remain liable for the payment and performance of all such liabilities and obligations, including, without limitation, any and all liabilities and obligations not assumed by the Owner Trustee or a Transferee pursuant to Section 4.01.

SECTION 5.02. Reimbursement. Unless a Default or an Event of Default shall have occurred and be continuing or an Event of Loss shall have occurred or a Deemed Loss Event shall have been declared, from and after the Lease Termination Date, upon the payment or performance by APS of any liability or obligation in respect of which the Owner Trustee shall also have become obligated in consequence of Article IV, and for so long as the Owner Trustee shall be so liable, APS shall be entitled to prompt reimbursement by the Owner Trustee for all amounts expended in connection with such payment or performance.

ARTICLE VI

FURTHER AGREEMENTS OF APS

SECTION 6.01. Agreement to Sell or Lease Unit 2 Retained Assets. Upon a transfer to a Transferee, APS agrees in respect of the Undivided Interest and the Real Property Interest, (i) if such Transferee is a purchaser of the Undivided Interest and the Real Property Interest, to sell to such Transferee, at a price equal to the Unit 2 Retained Assets Portion of the combined proceeds of the sale of the Undivided Interest and the undivided interest in the Unit 2

Retained Assets, an undivided interest, equal to the Unit 2 Interest, in and to the Unit 2 Retained Assets, or (ii) if the Transferee is a lessee of the Undivided Interest and the Real Property Interest, to lease to the Owner Trustee, at a rent equal to the Unit 2 Retained Assets Portion of the total rent received by the Owner Trustee from such Transferee, an undivided interest, equal to the Unit 2 Interest, in and to the Unit 2 Retained Assets, whereupon the Owner Trustee shall sublease or otherwise make available to such Transferee such undivided interest in and to such Unit 2 Retained Assets. Any such sale or lease by APS shall be accomplished by an appropriate bill of sale or lease.

SECTION 6.02. Agreement to Assign or Make Available ANPP Project Agreements. Upon a transfer to a Transferee, APS agrees in respect of the Undivided Interest and the Real Property Interest, (i) if the Transferee is a purchaser of the Undivided Interest and the Real Property Interest, to assign to such Transferee an undivided interest, equal to the Unit 2 Interest, in the ANPP Project Agreements (other than the ANPP Participation Agreement) to the extent relating to Unit 2 and the Unit 2 Retained Assets, and (ii) if such Transferee is a lessee of the Undivided Interest and the Real Property Interest, to assign for the term of such lease to such Transferee an undivided interest, equal to the Unit 2 Interest, in the ANPP Project Agreements (other than the ANPP Participation Agreement) to the extent relating to Unit 2 and the Unit 2 Retained Assets. Any assignment pursuant to this Section 6.02 shall be accomplished by an appropriate instrument of assignment.

SECTION 6.03. Agreements to Seek Amendments to the ANPP Participation Agreement and the License. The Lessee agrees to use its best efforts to obtain any required amendments to the ANPP Participation Agreement and the License to permit APS to act as Agent of the Owner Trustee in the manner contemplated by Section 7.01 hereof, if (i) APS shall not have elected to purchase the Undivided Interest as provided in Section 13(b) of the Facility Lease and (ii) there shall not be a Transferee in respect of the Undivided Interest and the Real Property Interest.

ARTICLE VII

INTERIM AGENCY ARRANGEMENTS

SECTION 7.01. Designation of Agent. From and after the Lease Termination Date (or during such period on or after the Lease Termination Date that the Owner Trustee shall have waived any Default or Event of Default with respect to the inability of the Lessee to surrender possession as required by Section 5(a) of the Facility Lease and until a transfer to a Transferee in respect of the Undivided Interest and the Real Property Interest (such period being referred to as the Agency Period), APS shall be, and the Owner Trustee hereby designates APS as, the initial agent (the Agent) of the Owner Trustee in the exercise of all rights assigned to the Owner Trustee hereunder. The Owner Trustee may terminate such agreement and the Agency Period at any time.

SECTION 7.02. Operation of Unit 2. During the Agency Period, the Agent shall administer the operation of the Undivided Interest and the Real Property Interest in accordance with this Agreement and all instructions of the Owner Trustee in accordance with Applicable Law. If, however, the Owner Trustee shall, prior to, or at any time during, the Agency Period, enter into any joint ownership and operating agreement with other Persons having a legal right to, or right to use, any other undivided interest in Unit 2, the Agent agrees to join in, and be bound by, the terms of such agreement if the Agent's performance thereunder shall not violate, or result in a violation of, any Applicable Law or the License. The Owner Trustee agrees to give the Agent reasonable prior written notice of the commencement of the negotiation of any such agreement.

SECTION 7.03. ANPP Participation Agreement. The Lessee agrees that, at all times during the Agency Period, it will perform all obligations and discharge all liability for which it is responsible as a "Participant" under the ANPP Participation Agreement in respect of the Undivided Interest and the Real Property Interest. In the performance of the foregoing agreement, APS shall have no obligation to exercise its rights as an ANPP Participant to cause Capital Improvements to be made to Unit 2 unless the Owner Trustee shall have agreed to provide funds for the payment of the Lessor's Portion of the cost of such

Capital Improvements to APS prior to the date on which such amounts shall be due with respect thereto under the ANPP Participation Agreement.

SECTION 7.04. Support. Except with respect to the Unit 2 Retained Assets for which provision is made in Section 7.06, APS covenants and agrees that, at all times during the Agency Period, it will provide, or make available, to the Owner Trustee such rights of the Lessee in and to other assets owned by APS and the ANPP Project Agreements, to the extent relating to the Undivided Interest and the Real Property Interest, as are necessary for the performance of the obligations of the Lessee hereunder.

SECTION 7.05. Compensation. As compensation for its obligations under Sections 7.02, 7.03 and 7.04, APS shall be entitled to receive, and the Owner Trustee hereby agrees to pay, an amount equal to (i) the Lessor's Portion of the aggregate of (A) amounts paid by APS as provided in Section 7.03 to the extent reasonably allocable to Unit 2 and (B) out-of-pocket expenses incurred by APS or the Agent, as the case may be, in connection with the performance of its agreements in this Article VII and (ii) the Unit 2 Retained Assets Portion of the net proceeds of the sale of power and energy in respect of Lessor's Portion of the Generation Entitlement Share. Compensation under (A) clause (i) of this Section 7.05 (which shall not exceed the fair market value for the obligations performed) shall be paid promptly in cash upon receipt of an invoice from APS and (B) clause (ii) of this Section 7.05 shall be paid promptly after receipt by the Owner Trustee.

SECTION 7.06. Transmission; Transmission Agreement. (a) The Lessee covenants and agrees that, at all times during the Agency Period, the Owner Trustee shall have the right to wheel, under normal transmission operating conditions, power and energy to which the Owner Trustee is entitled hereunder and under the other Transaction Documents and under the ANPP Participation Agreement, under normal transmission operating conditions, over transmission equipment in which APS now owns or may hereafter acquire an ownership interest, between Unit 2 and the ANPP Switchyard on terms and conditions no less favorable than those being offered to other similarly situated Persons.

(b) Based upon the respective rights, duties and obligations of the Owner Trustee and APS set forth in Section 7.06(a), if APS shall fail or decline to give the notice of renewal of the Facility Lease or purchase of the Undivided Interest, in each case as provided in Section 13(a) of the Facility Lease, APS and the Owner Trustee shall forthwith commence the negotiation in good faith of a definitive transmission agreement, not inconsistent with the terms and provisions of Section 7.06(a), but containing sufficient detail for the proper wheeling of power and energy, under normal transmission operating conditions, over the equipment of APS referred to in such Section 7.06(a) under then existing circumstances, for the exercise or stipulation, as the case may be, of the respective rights, duties and obligations of the Owner Trustee and APS set forth in Section 7.06(a). The Lessee and the Owner Trustee shall complete such negotiations and execute such definitive transmission agreement prior to the Lease Termination Date and such definitive transmission agreement shall provide for compensation to APS for the transmission services so provided at the Fair Market Sales Value thereof which, for purposes hereof, shall be determined with reference to the compensation then being paid by other similarly situated Persons for which the Lessee is providing such services.

ARTICLE VIII

MISCELLANEOUS

SECTION 8.01. Successors and Assigns. This Agreement shall be binding upon the successors and assigns of each of APS and the Owner Trustee.

SECTION 8.02. Governing Law. The interpretation of this Agreement and the rights and obligations of the parties hereto shall be governed by and construed and enforced in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

SECTION 8.03. Counterpart Execution. This Agreement may be executed in any number of counterparts and by each of the parties hereto on separate counterparts, all such counterparts together constituting but one and the same instrument.

SECTION 8.04. Amendments. The terms of this Agreement shall not be waived, altered, modified, amended, supplemented or terminated in any manner whatsoever, except by written instrument signed by APS and the Owner Trustee.

SECTION 8.05. Survival. All agreements and covenants contained in this Agreement or any agreement, document or certificate delivered pursuant hereto or in connection herewith shall survive the execution and delivery of this Agreement.

SECTION 8.06. Severability of Provisions. Any provision of this Agreement which may be determined by competent authority to be prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and no such prohibition or unenforceability in any jurisdiction shall invalidate or render unenforceable such provisions in any other jurisdiction. To the extent permitted by Applicable Law, APS hereby waives any provision of law which renders any provision hereof prohibited or unenforceable in any respect.

SECTION 8.07. Headings. The division of this Agreement into sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Agreement.

SECTION 8.08. Disclosure of Beneficiary. Pursuant to Arizona Revised Statutes §33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation, whose address is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts, 02110, Attention of Corporate Trust Division.

SECTION 8.09. Capacity of Lessee. Notwithstanding anything to the contrary in this Agreement, both parties hereto agree that all rights and obligations of the Lessee with respect to PVNGS under this Agreement are rights and obligations of the Lessee solely in its capacity as an ANPP Participant and not in its capacity as Operating Agent.

IN WITNESS WHEREOF, the parties hereto have #261
each caused this Agreement to be duly executed in New #262
York, New York by their respective officers thereunto #263
duly authorized. #(263)

ARIZONA PUBLIC SERVICE #266
COMPANY #(266)

By  #268
Paul A. Williams II #(268)

THE FIRST NATIONAL BANK OF #270
BOSTON, not in its individ- #271
ual capacity, but solely as #(271)
Owner Trustee under a Trust #272
Agreement, dated as of #(272)
August 1, 1986, with #(272)
Security Pacific Capital #(272)
Leasing Corporation #(272)

By: _____ #274
Assistant Vice President #(274)

IN WITNESS WHEREOF, the parties hereto have #261
each caused this Agreement to be duly executed in New #262
York, New York by their respective officers thereunto #263
duly authorized. # (263)

ARIZONA PUBLIC SERVICE #266
COMPANY # (266)

By: _____ #268
Paul A. Williams II # (268)

THE FIRST NATIONAL BANK OF #270
BOSTON, not in its individ- #271
ual capacity, but solely as # (271)
Owner Trustee under a Trust #272
Agreement, dated as of # (272)
August 1, 1986, with # (272)
Security Pacific Capital # (272)
Leasing Corporation. # (272)

By:  #274
Assistant Vice President # (274)

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Paul A. Williams II, a Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.

Anna Marie Napoli
Notary Public

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

ANNA MARIE NAPOLI
Notary Public, State of New York
No. 24-4759228
Qualified in Kings County
Certificate Filed in New York County
Commission Expires August 31, 19... 88

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Martin P. Henry, an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association under that certain Trust Agreement dated as of August 1, 1986.

Anna Marie Napoli
Notary Public

ANNA MARIE NAPOLI
Notary Public, State of New York
No. 24-4759228
Qualified in Kings County
Certificate Filed in New York County
Commission Expires August 31, 19... 88

When Recorded, Return to: David A. Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

AMENDMENT NO. 1

dated as of November 1, 1986

to

ASSIGNMENT, ASSUMPTION
AND
FURTHER AGREEMENT

dated as of August 1, 1986

between

ARIZONA PUBLIC SERVICE COMPANY

and

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity, but
solely as Owner Trustee under a
Trust Agreement with Security Pacific Capital Leasing Corporation

Original Assignment, Assumption and Further Agreement recorded on
August 18, 1986 as Instrument No. 86-439430 in Maricopa County,
Arizona Recorder's Office

AMENDMENT NO. 1, dated as of November 1, 1986, to the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), and THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (the Owner Trustee), under a Trust Agreement, dated as of November 1, 1986, with SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation, as Equity Participant (the Equity Participant).

WITNESSETH:

WHEREAS, the Lessee and the Owner Trustee have previously entered into an Assignment, Assumption and Further Agreement, dated as of November 1, 1986 (the Assignment and Assumption Agreement); and

WHEREAS, the Lessee and the Owner Trustee wish to amend the Assignment and Assumption Agreement as herein provided;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Amendments to Assignment and Assumption Agreement.

(a) Sections 3.01, 3.02 and 4.01 of the Assignment and Assumption Agreement are hereby amended by changing the phrase "Unit 2 Interest" to the phrase "Lessor's Portion".

(b) Sections 6.03(i) and 7.06(b) of the Assignment and Assumption Agreement are hereby amended by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest".

(c) Section 7.01 of the Assignment and Assumption Agreement is hereby amended by changing the phrase "as the Agency Period)" to the phrase "as the Agency Period))".

(d) Section 7.03 of the Assignment and Assumption Agreement is hereby amended by changing the phrase "Lessor's Portion" to the phrase "Unit 2 Interest".

(e) Section 7.05 of the Assignment and Assumption Agreement is hereby amended by changing the first sentence thereof to read in its entirety as follows:

"As compensation for its obligations under Sections 7.02, 7.03 and 7.04, APS shall be entitled to receive, and the Owner

Trustee hereby agrees to pay, in addition to the amounts described in the second sentence of Section 7.03, an amount equal to (i) the Lessor's Portion of out-of-pocket expenses incurred by APS or the Agent, as the case may be, in connection with the performance of its agreements in this Article VII and (ii) the Unit 2 Retained Assets Portion of the net proceeds of the sale of power and energy in respect of the Unit 2 Interest of the Generation Entitlement Share with respect to Unit 2."

(f) Appendix A to the Assignment and Assumption Agreement is hereby deleted and replaced by Appendix A attached hereto.

SECTION 2. Miscellaneous.

(a) Governing Law. The interpretation of this Amendment No. 1 and the rights and obligations of the parties hereto shall be governed by and construed and enforced in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

(b) Counterpart Execution. This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(c) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation. The address of the beneficiary is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to be duly executed in New York, New York by their respective officers thereunto duly authorized.

ARIZONA PUBLIC SERVICE COMPANY

By: [Signature]
Vice President and Treasurer

Date: November 19, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner Trustee

By: [Signature]
Assistant Vice President

Date: November 19, 1986

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986 by PAUL A. WILLIAMS II, Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.

David A. Spivak

Notary Public

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4633488
Qualified in New York County
Commission Expires March 30, 1988

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under the Trust Agreement dated as of August 1, 1986 with Security Pacific Capital Leasing Corporation.

David A. Spivak

Notary Public

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4633488
Qualified in New York County
Commission Expires March 30, 1988

When recorded, return to:

David Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

DEED AND BILL OF SALE .

Dated as of August 18, 1986

between

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona corporation,
as Seller

and

THE FIRST NATIONAL BANK OF BOSTON, a national banking
association, not in its individual capacity, but solely
as Owner Trustee under a Trust Agreement, dated as of
August 1, 1986, with Security Pacific Capital Leasing
Corporation,
as Buyer

DEED AND BILL OF SALE, dated as of August 18, 1986 between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Seller), and THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as Owner Trustee (in such capacity, the Owner Trustee) under the Trust Agreement, dated as of August 1, 1986, with the Equity Participant identified in paragraph 6 hereof (the Owner Trustee in its capacity as owner trustee under the foregoing Trust Agreement being hereinafter referred to as the Buyer).

W I T N E S S E T H :

WHEREAS, the Seller desires to sell, and the Buyer desires to purchase, the Undivided Interest, for and in consideration of the amounts paid by the Buyer to the Seller pursuant to the Participation Agreement (as hereinafter defined);

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

1. For the purpose hereof, capitalized terms used herein, unless otherwise defined herein, shall have the meanings assigned to such terms in Appendix A attached hereto.

The property described in Exhibit B hereto is collectively referred to herein as Unit 2 and the undivided interests therein being conveyed pursuant hereto are referred to collectively herein as the Undivided Interest. Unit 2 is located on the PVNGS Site described in Exhibit A hereto.

2. The Seller does hereby GRANT, BARGAIN, CONVEY, SELL, ASSIGN, TRANSFER AND SET OVER unto the Buyer a 3.6955% undivided interest in Unit 2 TO HAVE AND TO HOLD the same unto the Buyer, its successors and assigns, FOREVER. It is the intent of this Deed and Bill of Sale, that, from and after the date of this Deed and Bill of Sale, Buyer will own a 3.6955% undivided interest in Unit 2, as a tenant in common with the owners of the remaining undivided interests in Unit 2.

3. The Seller does hereby WARRANT AND COVENANT that it is the true and lawful owner of the Undivided Interest and has good right to sell the Undivided Interest, that title to the Undivided Interest is on the date of execution hereof free and clear of all claims, liens, security interests and encumbrances of any nature, other than Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition of such term) and Liens for 1986 taxes not yet due and payable that good, marketable and indefeasible title to the Undivided Interest is hereby conveyed to the Buyer, and that the Seller will forever warrant and defend such title against the claims of all Persons. The foregoing warranties of the Seller are to

the restraint of any other covenant of the Seller otherwise arising by implication by virtue of Arizona Revised Statutes, Section 33-435.

4. The Seller and the Buyer hereby acknowledge and confirm that, as between the Seller and the Buyer, the Undivided Interest is and will remain personal property, and is not, and will not become, an accession to the PVNGS Site or to the Real Property Interest, title thereto being separate and distinct from title to such real property. The Buyer hereby waives any rights it may have to partition Unit 2, including the Undivided Interest, whether by partitionment in kind or by sale and division of proceeds, and further agrees that it will not resort to any action in law or in equity to partition Unit 2 and it waives the benefits of all laws that may now or hereafter authorize such partition for a term (i) which shall be coterminous with the ANPP Participation Agreement or (ii) which shall be for such lesser period as may be required by Applicable Law.

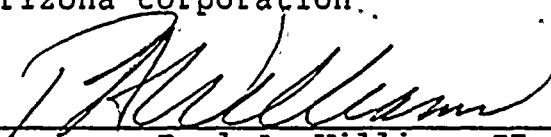
5. Pursuant to the Assignment and Assumption, the Seller has agreed to pay certain costs and expenses relating to Unit 2, including, but without limitation, with respect to decommissioning and retirement of Unit 2, and to perform and comply with certain obligations relating to transfers of interests in Unit 2. All such agreements and obligations of the Seller are hereby incorporated by reference in this Deed and Bill of Sale as if set forth in full herein.

6. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation (the Equity Participant), whose address is Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts, 02110, Attention of Corporate Trust Division.

IN WITNESS WHEREOF, the parties hereto have caused this Deed and Bill of Sale to be executed as of this 18th day of August.

ARIZONA PUBLIC SERVICE COMPANY, an
Arizona corporation.

By



Paul A. Williams II

THE FIRST NATIONAL BANK OF BOSTON, a
national banking association, not in
its individual capacity, but solely as
Owner Trustee under the Trust Agreement

By

Assistant Vice President

IN WITNESS WHEREOF, the parties hereto have caused this Deed and Bill of Sale to be executed as of this 18th day of August.

ARIZONA PUBLIC SERVICE COMPANY, an
Arizona corporation

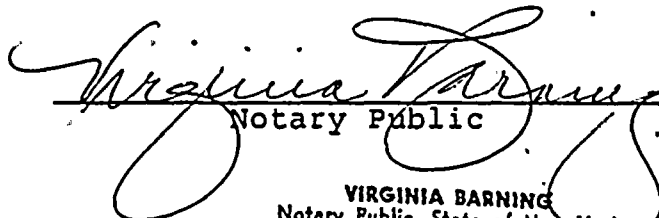
By _____
Paul A. Williams II

THE FIRST NATIONAL BANK OF BOSTON, a
national banking association, not in
its individual capacity, but solely as
Owner Trustee under the Trust Agreement

By _____
Assistant Vice President

State of New York)
) ss:
County of New York)

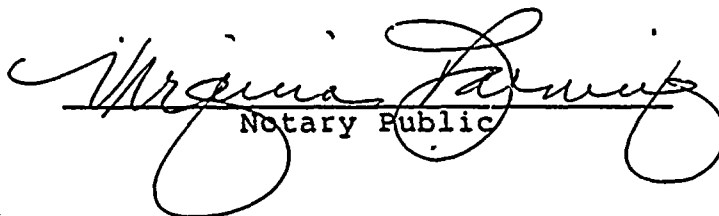
The foregoing instrument was acknowledged before me this 18th day of August, 1986, by PAUL A. WILLIAMS II, the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.


Notary Public

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified In Kings County
Certificate filed In New York County
Commission Expires March 30, 1988

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as trustee under that certain Trust Agreement dated as of August 1, 1986.


Notary Public

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified In Kings County
Certificate filed In New York County
Commission Expires March 30, 1988

EXHIBIT A
to
DEED AND
BILL OF SALE

PVNGS SITE DESCRIPTION

PARCEL NO. 1: Lot Four (4); the Southwest quarter of the Northwest quarter; and the West half of the Southwest quarter, all in Section Two (2), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 2: All of Section Three (3), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 3: The East half of Section Four (4), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 4: The West half of Section Twenty-six (26), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 5: Section Twenty-seven (27), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter of Section 27.

PARCEL NO. 6: The Southeast quarter of Section Twenty-eight (28), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT 50% of all oil, gas and other mineral deposits and geothermal resources recovered from or developed on the property, as reserved in instrument recorded May 10, 1974 in Docket 10647, page 136.

PARCEL NO. 7: The East half of Section Thirty-three (33), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 8: All of Section Thirty-four (34), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 9: The West half of Section Thirty-five (35), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 10: The Southeast quarter of Section Nine (9), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and

Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter thereof.

PARCEL NO. 11: All of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the East half of the Southeast quarter thereof; and EXCEPT the North half of the South half of the Northwest quarter of the Northwest quarter thereof.

PARCEL NO. 12: That part of the East half of the Southwest quarter of Section Twenty-three (23), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona, more particularly described as follows:

BEGINNING at the Southeast corner of the said East half of the Southwest quarter of Section 23; thence West, an assumed bearing along the South line of the said East half of the Southwest quarter of Section 23, for a distance of 762.04 feet; thence North 0 degrees 03 minutes 39 seconds West; parallel to the East line of the said East half of the Southwest quarter of Section 23, for a distance of 1946.46 feet to a point on the South right-of-way line of the 200 foot wide HASSAYAMPA-SALOME HIGHWAY, as recorded in Book 12 of Road Maps, page 82, Maricopa County Recorder, Maricopa County, Arizona; thence continuing North 0 degrees 03 minutes 39 seconds West for a distance of 234.15 feet to a point on the North right-of-way line of said highway; thence South 58 degrees 43 minutes 35 seconds East, along said North right-of-way line for a distance of 892.17 feet to a point on the said East line of the East half of the Southwest quarter of Section 23; thence South 0 degrees 03 minutes 39 seconds East, along said East line for a distance of 234.15 feet to a point on the said South right-of-way line; thence continuing South 0 degrees 03 minutes 39 seconds East for a distance of 1483.31 feet to the true point of beginning;

EXCEPT the East 305 feet of the South 305 feet thereof; and

EXCEPT one-half of the minerals and mineral rights and mineral estates of every kind and nature, as set forth in Deed recorded in Docket 11652, page 52, Maricopa County Records.

PARCEL NO. 13: The North half of the South half of the Northwest quarter of the Northwest quarter of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

EXHIBIT B
to
DEED AND
BILL OF SALE

UNIT 2 DESCRIPTION

Unit 2 of the Palo Verde Nuclear Generating Station (PVNGS), located in Maricopa County, Arizona, approximately 55 miles west of the City of Phoenix, Arizona, and approximately 16 miles west of the City of Buckeye, Arizona, consisting of:

- I. Unit 2 Combustion Engineering "System 80" pressurized water reactor nuclear steam supply system (the NSSS). The NSSS is comprised of a reactor vessel containing 241 fuel assemblies with approximately 100 tons of enriched uranium (fuel assemblies, however, are not part of Unit 2 and are not included in the Undivided Interest being sold), two steam generators, four reactor coolant pumps and various additional systems and subsystems. The licensed thermal rating of the NSSS is 3800 MW.
- II. Unit 2 GE TC6F-43, 1800 RPM tandem-compound, six flow, reheat turbine-generator including turbine, generator, moisture separator-reheater, exciter, controls, and auxiliary subsystems. The turbine-generator is conductor cooled and rated at 1,554 MVA at 24,000 V, 3 phase, 60 Hz, 1.5 in Hg ABS back pressure, and approximately 1,363 MW maximum gross electric output.
- III. Unit 2 146 ft. inside diameter, steel-lined, prestressed concrete cylindrical containment building with a hemispherical dome designed for 60 psig. The containment building houses the reactor system.
- IV. Unit 2 auxiliary systems and equipment including engineered safeguards systems, reactor auxiliary systems and turbine-generator auxiliary systems associated with items I, II, and III above, extending to and including the Unit 2 start-up transformer.
- V. Unit 2 cooling tower system consisting of three (3) mechanical draft cooling towers, including a closed cycle circulating water system, make-up water systems and essential spray ponds.

- VI. Unit 2 radioactive waste treatment system, including liquid, gaseous, and solid waste subsystems, controls, instrumentation, storage, handling and shipment facilities.
- VII. Unit 2 emergency diesel-generator system, including a diesel-generator building which contains two diesel generators, fuel oil systems, storage tanks, control and instrumentation systems and other equipment.
- VIII. Unit 2 internal communication systems, including associated interconnections and computer data links.

BUT EXCLUDING:

- I. Nuclear fuel for Unit 2, including spare fuel assemblies, and nuclear waste.
- II. Spare Parts (Unit 2).
- III. Transmission facilities (including any and all facilities and equipment providing interconnection between the Unit 2 turbine generator and the ANPP High Voltage Switchyard, including step-up transformers and standby equipment and systems).
- IV. Oil and diesel fuel inventories (Unit 2).

When recorded, return to: David Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

DEED

For the consideration of Ten Dollars (\$10.00) and other valuable considerations, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (Grantor), hereby grants, conveys, sells, transfers and assigns to THE FIRST NATIONAL BANK OF BOSTON, a national banking association, as Owner Trustee (the Owner Trustee) under that certain Trust Agreement (the Trust Agreement), with the beneficiary identified below, dated as of August 1, 1986 (the Owner Trustee being hereinafter referred to as Grantee), until the commencement of Decommissioning, as such term is defined in Appendix A attached hereto, an undivided 1.23% interest in the land that is more particularly described in Exhibit A attached hereto and by this reference incorporated herein (the Land), together with all rights and privileges of Grantor appurtenant thereto, including but not limited to the perpetual (subject to the Possibility of Reversion, as hereinafter defined) right to locate, maintain and use the Improvements (as hereinafter defined) on the Land and the perpetual (subject to the Possibility of Reversion) right of ingress and egress over, upon and across the Land to the Improvements, BUT excepting and excluding from the transfer being made pursuant to this Deed any and all facilities, structures, improvements, equipment and property of whatever kind and nature now or hereafter constructed, placed or affixed on the Land (collectively, the Improvements), Grantor and Grantee hereby acknowledging and agreeing that the interest in the Improvements was acquired by Grantee pursuant to a separate Deed and Bill of Sale dated as of August 18, 1986, between Grantor and Grantee and not pursuant to this Deed.

I. The interest being transferred pursuant to this Deed is subject to the ANPP Participation Agreement (as such term is defined in Appendix A attached hereto), the Project Agreements (as defined in said ANPP

Participation Agreement), any Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition thereof in Appendix A attached hereto and to the matters set forth in Exhibit B attached hereto and incorporated herein by this reference.

II. Grantor hereby warrants that it is the true and lawful owner of the undivided interest conveyed hereby in the property described in Exhibit A attached hereto and has good right to sell the undivided interest in such property; that Grantor has good and marketable title to the undivided interest in the property described in Exhibit A and that title to such property is on the date of execution hereof free and clear of all claims, liens, encumbrances, security interests, covenants, assessments, rights, reservations, easements, restrictions and conditions save and except only any Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition thereof in Appendix A attached hereto and those matters set forth in Exhibit B attached hereto. Grantor hereby warrants that good and marketable title to the undivided interest in the property described in Exhibit A is hereby conveyed to Owner Trustee subject only to the Possibility of Reversion; and that the title to the undivided interest in the property described in Exhibit A conveyed to the Owner Trustee is determinable only to the extent that such title shall automatically terminate and revert to the Grantor, its successors and assigns, without any further act or deed by any person whatsoever upon the commencement of Decommissioning (such possibility of automatic termination and reversion being herein referred to as the Possibility of Reversion). Subject only to the Possibility of Reversion and to the matters set forth in Exhibit B attached hereto, Grantor hereby warrants, and will forever defend, the title against all persons whomsoever. Any attempt by Grantor, its successors and assigns, to terminate the Possibility of Reversion shall be null, void and of no force or effect whatsoever.

III. Grantor intends by this Deed that, from and after the recordation of this Deed, but subject to the Possibility of Reversion, Grantee will own an undivided 1.23% interest in the property described in Exhibit A, as a tenant in common with the owners of the remaining undivided interests in such property.

IV. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Security Pacific Capital Leasing Corporation, a Delaware corporation, Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Attention: Manager, Operations Department/LEV. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.


IN WITNESS WHEREOF, Grantor has caused this Deed to be executed as of the 18th day of August, 1986.

ARIZONA PUBLIC SERVICE
COMPANY,
an Arizona corporation

By 
Vice President and Treasurer

ACCEPTED AND AGREED TO:

The First National Bank of Boston,
a national banking association,
not in its individual capacity, but
solely as Trustee of the Trust
Agreement.

By 
Assistant Vice President

STATE OF NEW YORK)
) ss.
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Paul A. Williams II, Vice President and Treasurer of Arizona Public Service Company an Arizona corporation, on behalf of the corporation.

Delia T. Santiago
Notary Public

My Commission Expires:

CELIA T. SANTIAGO
Notary Public, State of New York
No. 41-3451160
Qualified in Queens County
Commission Expires March 30, 1989

STATE OF NEW YORK)
) ss.
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Martin P. Henry, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under that certain Trust Agreement dated as of August 1, 1986.

Delia T. Santiago
Notary Public

CELIA T. SANTIAGO
Notary Public, State of New York
No. 41-3451160
Qualified in Queens County
Commission Expires March 30, 1989

EXHIBIT A
to
DEED

PVNGS SITE DESCRIPTION

PARCEL NO. 1: Lot Four (4); the Southwest quarter of the Northwest quarter; and the West half of the Southwest quarter, all in Section Two (2), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 2: All of Section Three (3), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 3: The East half of Section Four (4), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 4: The West half of Section Twenty-six (26), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 5: Section Twenty-seven (27), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter of Section 27.

PARCEL NO. 6: The Southeast quarter of Section Twenty-eight (28), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT 50% of all oil, gas and other mineral deposits and geothermal resources recovered from or developed on the property, as reserved in instrument recorded May 10, 1974 in Docket 10647, page 136.

PARCEL NO. 7: The East half of Section Thirty-three (33), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 8: All of Section Thirty-four (34), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 9: The West half of Section Thirty-five (35), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 10: The Southeast quarter of Section Nine (9), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter thereof.

PARCEL NO. 11: All of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the East half of the Southeast quarter thereof; and EXCEPT the North half of the South half of the Northwest quarter of the Northwest quarter thereof.

PARCEL NO. 12: That part of the East half of the Southwest quarter of Section Twenty-three (23), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona, more particularly described as follows:

BEGINNING at the Southeast corner of the said East half of the Southwest quarter of Section 23; thence West, an assumed bearing along the South line of the said East half of the Southwest quarter of Section 23, for a distance of 762.04 feet; thence North 0 degrees 03 minutes 39 seconds West; parallel to the East line of the said East half of the Southwest quarter of Section 23, for a distance of 1946.46 feet to a point on the South right-of-way line of the 200 foot wide HASSAYAMPA-SALOME HIGHWAY, as recorded in Book 12 of Road Maps, page 82, Maricopa County Recorder, Maricopa County, Arizona; thence continuing North 0 degrees 03 minutes 39 seconds West for a distance of 234.15 feet to a point on the North right-of-way line of said highway; thence South 58 degrees 43 minutes 35 seconds East, along said North right-of-way line for a distance of 892.17 feet to a point on the said East line of the East half of the Southwest quarter of Section 23; thence South 0 degrees 03 minutes 39 seconds East, along said East line for a distance of 234.15 feet to a point on the said South right-of-way line; thence continuing South 0 degrees 03 minutes 39 seconds East for a distance of 1483.31 feet to the true point of beginning;

EXCEPT the East 305 feet of the South 305 feet thereof; and

EXCEPT one-half of the minerals and mineral rights and mineral estates of every kind and nature, as set forth in Deed recorded in Docket 11652, page 52, Maricopa County Records.

PARCEL NO. 13: The North half of the South half of the Northwest quarter of the Northwest quarter of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

EXHIBIT B
to
DEED

1. The right to enter upon, occupy and use, any part or all of that portion of the West half of the West half of Section 27, lying within 20 feet of the center line of the transmission line right of way of the Central Arizona Light and Power Company for the purposes provided in the Act of June 10, 1920 (41 STAT., 1063), and subject to the conditions and limitations of Section 24 of said Act, as amended by the Act of August 26, 1935 (49 STAT., 846), as reserved unto the United States of America in instrument recorded September 30, 1949 in Docket 442, page 577. (Part of Parcel 5 - South half of said Section 27)

2. Roadway over the South 65 feet of said Sections 9 and 10, as shown on Book 13 of Road Maps, page 48. (Parcels 10 and 11)

3. Easement and rights incident thereto for electric lines approximately 28 feet South of the North line of said Section 34, as set forth in instrument recorded February 20, 1952 in Docket 878, page 548. (Parcel No. 8)

4. All the Oil and Gas in said lands, as reserved unto the United States of America, and the right to prospect for, mine and remove such deposits from the same upon compliance with the conditions and subject to the provisions and limitations of the Act of June 17, 1914 (38 Stat. 509), as set forth in Patent recorded June 4, 1957 in Docket 2194, page 409. (Part of Parcel No. 11)

5. Easement and rights incident thereto for transmission line over said Section 34, said easement being 10 feet in width, the centerline described as follows: Beginning at a point approximately 28 feet South and 2445.5 feet East of the Northwest corner of said Section 34; thence Southerly along, parallel to and approximately 2620 feet to a point; thence Easterly along, parallel to, and approximately 2648 feet South of the North line of said Section 34, a distance of approximately 1556 feet to a point, as set forth in instrument recorded January 15, 1962 in Docket 3992, page 49. (Parcel No. 8)

6. One-Sixteenth of all gas, oil, metals and mineral rights as reserved unto the State of Arizona, in Patent recorded January 11, 1974 in Docket 10473, page 447. (Parcel 1)

7. Easement and rights incidents thereto for highway purposes over the West 55 feet of the East half of said Section 4, as set forth in the instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 3)

8. Easement and rights incident thereto for highway purposes over the West 55 feet of the Southeast quarter of said Section 28, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 6)

9. Easement and rights incident thereto for highway purposes over the West 55 feet of the East half of said Section 33, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 7)

10. Easement and rights incident thereto for highway purposes over the West 55 feet of the Southeast quarter of said Section 9, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Part of Parcel 10)

11. Easement and rights incident thereto for electric lines over the North 10 feet of the following described property: The Southeast quarter of Section 28, Township 1 North, Range 6 West Except the West 55 feet thereof for roadway, as set forth in instrument recorded June 25, 1976 in Docket 11736, page 1089. (Parcel 6)

12. Easement for highway purposes over said premises, as granted to Maricopa County, a Political Subdivision, by instrument recorded December 15, 1977 in Docket 12602, page 575, described as follows: The South 40 feet of the East one-half of the Southeast quarter of Section 9; the South 40 feet of the Southwest quarter of Section 10; the South 40 feet of the West one-half of the Southeast quarter of Section 10, the South 40 feet of the Southwest quarter of the Southeast quarter of Section 9; All being in Township 1 South, Range 6 West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

13. A roadway of a width consistent with the right of way over the Southerly portion of Sections 9 and 10 of the within described property, and other property designated County Road on Book 25 of Road Maps, page 47, recorded December 26, 1978. (Also known as Ward Road from the Hassayampa Salome Highway to the South entrance of the Palo Verde Nuclear Generating Station)

14. 1986 taxes not yet due and payable.

15. Easement and rights incident thereto for transmission line over a portion of said premises, as set forth in instrument recorded November 15, 1985 in Document No. 85-544604. (Parcels 1, 2, 8, 9 and 11)

16. Easement and rights incident thereto for highway over a portion of said premises, as set forth in instrument recorded February 3, 1959 in Docket 2740, page 309, and as shown in Book 12 of Road Maps, page 82 (Parcel 12).

17. Easement and rights incident thereto for roadway 20 feet in width, over the East 20 feet of the within described property, by instrument recorded October 19, 1976, in Docket 11907, page 115 (Parcel 12).

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof", "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the Initial Series Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive or accrued) of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or

determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 14(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under any Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York, Boston, Massachusetts or San Francisco, California are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement, is or is not included or reflected in the plans and specifications for Unit 2, as built, and (b) any alteration, modification, addition or improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of

the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date.. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any Basic Rent Payment Date, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation) of any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean a Collateral Trust Indenture among APS, Funding Corp and the Collateral Trust Trustee in form and substance satisfactory to APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS common facilities which are common to all generating units, including Unit 2, at PVNGS.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original

term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning in respect of Unit 2 and the Unit 2 Retained Assets (including, without limitation, the Common Facilities and the PVNGS Site allocable to Unit 2) set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in Exhibit A to the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deemed Loss Events shall mean [to be supplied by amendment].

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank (as used herein, an Issuing Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Issuing Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Issuing Bank, or (iii) any Issuing Bank whose long-term unsecured debt securities are rated not less than Aa3 by Moody's, other than an Issuing Bank to which the Equity

Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of an Issuing Bank which is part of a holding company structure, the failure of such Issuing Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities; provided, however, that any Letter of Credit issued by an Issuing Bank that is not incorporated in the United States shall provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Security Pacific Capital Leasing Corporation, and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended.

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean [to be supplied by amendment].

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and interest with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank, together with thirty-seven indentures supplemental thereto.

Extraordinary Casualty Value, as of any Basic Rent Payment Date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any Basic Rent Payment Date, the aggregate unpaid principal amount of all Notes Outstanding at the close

of business on such date, together with accrued and unpaid interest on such Notes.

Facility Cost shall mean the Purchase Price plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement, and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended.

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x)(A) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; or (B) any order of or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period which will exceed 24 months or (y) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the

primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) assessment of core damage according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2 containment (as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date) (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples, which indicate that the damage to the nuclear fuel residing in the reactor vessel is in categories 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9, or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which (x) the NRC declares to be an Extraordinary Nuclear Occurrence (as such term is defined in the Atomic Energy Act); (y) results in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber), or such alternative standards as

may hereafter be adopted by the NRC with respect to the radiation levels required for the occurrence of an Extraordinary Nuclear Occurrence and determined by the Lessee and the Equity Participant to be equivalent to the standards which were applicable hereunder prior to the adoption by the NRC of such alternative standards; provided, however, that if the NRC shall reduce any level of measurement, if either the Extraordinary Nuclear Occurrence Criteria for off site contamination are reduced by NRC as set forth above or alternative criteria are adopted by NRC, then the levels herein shall be reduced or modified so as to be consistent with the reduction by the NRC; or (z) results in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination, estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building above such storage facility, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee, or of the Lessee and one or more other ANPP Participants to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than

three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown declared in consequence of the occurrence of an event described in (A) clauses 3 and 4 above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause 7 above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months.

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meanings set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, the Generation Entitlement Share of AFS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all siting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, the Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles, a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean that portion of APS's interest in Unit 2 equal to the percentage set forth on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the

Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended, (vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of (x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of such Fixed Rate Renewal Term) in each case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and

(iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or the December 30 in the last twelve months of such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage.

Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions.

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest on or after the Lease Termination Date or (iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes, Refunding Notes and Additional Notes issued from time to time in registered form under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act; provided that if the Atomic Energy Act shall be amended after the date hereof to expand the definition of "nuclear incident", the meaning of Nuclear Incident shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used or by a Contract Administrator.

Original Loan Participants shall mean Bank of America and each of the other banks listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs) or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participant and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part

thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest) under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No. 85-256, 71 Stat. 576 (1957), as amended to August 18, 1986, including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 2 to the Participation Agreement.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Insurance shall have the meaning assigned thereto in the ANPP Participation Agreement.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund Outstanding Notes.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean the Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of the Refunding Bonds.

Registration Statement shall mean the registration statement on Form S-3, including all exhibits and all documents incorporated in the Registration Statement by reference, to be filed with the SEC under the Securities Act in connection with the offer, issue and sale of the Refunding Bonds.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12 of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent..

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Severable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor and the Equity Participant in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 19(i)(1) of the Participation Agreement.

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining a residual of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted security ratings.

Summary Statement shall have the meaning set forth in Section 19(i) of the Participation Agreement.

Substituted Lessee shall have the meaning set forth in Section 6.8(b) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Lessor.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property, (personal or real, tangible or intangible), and stamp taxes), levies, imposts, duties, charges, assessments, or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon.

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed by an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Security Pacific Capital Leasing Corporation and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp, APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale, (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP High Voltage Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common

facilities); (xiii) simulator; and (xiv) oil and diesel fuel inventories, (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements, and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii) railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

COLLATERAL TRUST INDENTURE

dated as of November 1, 1986

AMONG

PVNGS FUNDING CORP., INC.,

ARIZONA PUBLIC SERVICE COMPANY

AND

CHEMICAL BANK,
as Trustee

**Providing for the Issuance from Time to Time of
Securities To Be Issued in One or More Series**

PALO VERDE NUCLEAR GENERATING STATION

PVNGS FUNDING CORP., INC.
ARIZONA PUBLIC SERVICE COMPANY

Reconciliation and tie between Indenture
dated as of , 1986

and

Trust Indenture Act of 1939

<u>Section of Act</u>	<u>Section of Indenture</u>
310(a)(1)	9.09
(2)	9.09
(3)	Inapplicable
(4)	Inapplicable
(b)	9.08, 9.10(a), 9.10(d), 9.10(e), 9.11
(c)	Inapplicable
311(a)(b)	9.13
(c)	Inapplicable
312(a)	10.01
(b)	10.02(a)
(c)	10.02(b)
(d)	10.02(c)
313(a)	10.03(a)
313(b)(1)	10.03(b)(1)
(2)	10.03(b)
(c)	10.03(a) & (b)
(d)	10.03(c)
314(a)	10.04
(b)	5.06
(c)(1)	1.02
(2)	1.02
(3)	2.04(7)(A)
(d)(1)	5.11, 5.12
(2)	Inapplicable
(3)	2.04(7)(B)
(e)	1.02
315(a)(1)	9.01(a)(1)
(2)	9.01(a)(2)
315(a)(last clause)	9.01(a)(2)
(b)	9.02
(c)	9.01(b)
(d)(1)	9.01(c)(1)

<u>Section of Act</u>	<u>Section of Indenture</u>
(2)	9.01(c)(2)
(3)	9.01(c)(3)
(e)	8.10
316(a)(1)(A)	8.07
(B)	8.08
(2)	Inapplicable
(a) (last sentence)	1.01 ("Outstanding")
(b)	8.11
317(a)(1)	8.05(a)
(2)	8.05(d)
(b)	5.03
(c)(2)	9.14
318(a)	1.07

NOTE: This reconciliation and tie shall not, for any purpose, be deemed to constitute a part of the Indenture.

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PARTIES

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COLLATERAL TRUST INDENTURE, dated as of November 1, 1986, among PVNGS FUNDING CORP., INC., a Delaware corporation (hereinafter called the *Company*), having its principal office and mailing address at Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 19801, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, having its principal office and mailing address at 411 North Central Avenue, Phoenix, Arizona 85072-3999 (hereinafter called *APS*), and CHEMICAL BANK, a New York banking corporation, as Trustee (hereinafter called the *Trustee*), having its corporate trust office at 55 Water Street, New York, New York 10041.

RECITALS

WHEREAS, the Company has duly authorized the creation of an issue of its debentures, notes or other evidences of indebtedness to be issued in one or more series (the *Securities*) up to such principal amount or amounts as may from time to time be authorized in accordance with the terms of this Indenture; and to secure the Securities and to provide for the authentication and delivery thereof by the Trustee, the Company has duly authorized the execution and delivery of this Indenture; and

WHEREAS, all acts necessary to make this Indenture a valid instrument for the security of the Securities, in accordance with its and their terms, have been done;

NOW, THEREFORE, THIS INDENTURE WITNESSETH, that, to secure the payment of the principal of, and premium (if any) and interest on, all the Securities authenticated and delivered hereunder and issued by the Company and outstanding, and the performance of the covenants therein and herein contained, and in consideration of the premises and of the covenants herein contained and of the purchase of the Securities by the holders thereof, and of the sum of one dollar (\$1.00) paid to the Company by the Trustee at or before the delivery hereof, the receipt whereof is hereby acknowledged, the Company by these presents does grant, bargain, sell, release, convey, assign, pledge, transfer, mortgage, hypothecate, and confirm unto the Trustee all and singular the following (which collectively are hereinafter called the *Pledged Property*), excluding, in any event, any moneys which are specifically stated herein not to constitute part of the Pledged Property, to wit:

CLAUSE FIRST

All Pledged Lessor Notes (as hereinafter defined) as shall be actually pledged and assigned by the Company to the Trustee pursuant to the Series Supplemental Indentures or other supplemental indentures to be executed and delivered as provided in this Indenture, together with the interest of the Company (if any) in the Lease Indentures (as hereinafter defined) securing said Pledged Lessor Notes.

CLAUSE SECOND

All right, title and interest of the Company in, to and under any agreements with respect to commitment fees or other amounts payable by APS entered into between APS and the Company in connection with the issuance and sale of any series of Securities, if actually assigned by the Company to the Trustee pursuant to a Series Supplemental Indenture or other supplemental indentures to be executed and delivered as provided in this Indenture.

CLAUSE THIRD

All the proceeds received by the Company from the sale of the Securities, all the tolls, rents, issues, profits, products, revenues and other income of the property subjected or required to be subjected to the lien of this Indenture, and all the estate, right, title and interest of every nature whatsoever of the Company in and to the same and every part thereof.

CLAUSE FOURTH

Any property, including cash, that may, from time to time hereafter be subjected to the lien and/or pledge hereof by the Company or which pursuant to any provision of this Indenture or any Series Supplemental Indenture or other supplemental indentures to be executed and delivered as provided in this Indenture may become subjected to the lien and/or pledge hereof; and the Trustee is hereby authorized to receive the same at any time as additional security hereunder. Such subjection to the lien hereof of any such property as additional security may be made subject to any reservations, limitations or conditions which shall be set forth in a written instrument executed by the Company and/or by the Trustee respecting the scope or priority of such lien and/or pledge or the use and disposition of such property or the proceeds thereof.

TO HAVE AND TO HOLD the Pledged Property unto the Trustee and its successors and assigns forever subject to the terms of this Indenture, including, without limitation, Section 12.01.-

BUT IN TRUST, NEVERTHELESS, for the equal and proportionate benefit and security of the holders from time to time of all the Securities authenticated and delivered hereunder and issued by the Company and outstanding, without any priority of any one Security over any other.

AND UPON THE TRUSTS and subject to the covenants and conditions hereinafter set forth.

ARTICLE ONE

DEFINITIONS AND OTHER PROVISIONS OF GENERAL APPLICATION.

SECTION 1.01. *Definitions.*

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

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

(2) all other terms used herein which are defined in the Trust Indenture Act (as hereinafter defined), either directly or by reference therein, have the meanings assigned to them therein;

(3) all accounting terms not otherwise defined herein have the meanings assigned to them in accordance with generally accepted accounting principles;

(4) all reference in this Indenture to designated "Articles", "Sections" and other subdivisions are to the designated Articles, Sections and other subdivisions of this Indenture; and

(5) 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.

Certain terms, used principally in Article Nine, are defined in that Article.

"Act" when used with respect to any Holder has the meaning specified in Section 1.04.

"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.

"APS" means Arizona Public Service Company, an Arizona corporation, and, subject to the provisions hereof, its successors and assigns.

"Authorized Agent" means any Paying Agent or Security Registrar or other agent appointed by the Trustee in accordance with this Indenture to perform any function which this Indenture authorizes the Trustee or such agent to perform.

"Board of Directors" means the board of directors of the Company, when used with respect to the Company, and either the board of directors, or any committee of that board duly authorized to act for it hereunder, when used with respect to APS.

"Board Resolution" means a copy of a resolution certified by the Secretary, an Assistant Secretary or an Associate Secretary of the Company or APS, as the case may be, to have been duly adopted by the Board of Directors of such entity and to be in full force and effect on the date of such certification, and delivered to the Trustee.

"Business Day" means any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York or Boston, Massachusetts are authorized or obligated to be closed.

"Change" with respect to any instrument means any consent, amendment, waiver, approval, notice or direction or the execution, grant or giving of any thereof.

"Commission" means the Securities and Exchange Commission, as from time to time constituted, created under the Securities Exchange Act of 1934, 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 on such date.

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

"Company Request" and *"Company Order"* mean, respectively, a written request or order signed in the name of the Company by its President or one of its Vice Presidents, and by its Treasurer, Secretary, or one of its Assistant Treasurers or Assistant Secretaries or Associate Secretaries, and delivered to the Trustee.

"Corporate Trust Office" means the principal office of the Trustee at which at any particular time corporate trust business of the Trustee shall be administered, which at the date of this Indenture is 55 Water Street, New York, N.Y. 10041, Attention: Corporate Trustee Administration.

"Equity Participant" means any Equity Participant identified in a Schedule to a Series Supplemental Indenture, until a successor or assignees thereof shall have become such pursuant to the applicable provisions of the Participation Agreement to which such Equity Participant is a party, and thereafter *"Equity Participant"* means such successor or assignees; *"Equity Participants"* means each and every Equity Participant.

"Event of Default" has the meaning specified in Section 8.01.

"Extension Letter" means the Extension Letter, to be dated the date of issue of a Pledged Lessor Note and addressed to the Trustee by the parties to the Participation Agreement pursuant to which such Pledged Lessor Note was issued, extending to the Trustee the representations, warranties and covenants of such parties set forth in such Participation Agreement.

"Holder" or *"Securityholder"* means a Person in whose name a Security is registered in the Security Register.

"Indenture" means this instrument as originally executed and as it may from time to time be supplemented or amended by one or more indentures supplemental hereto entered into pursuant to the applicable provisions hereof.

"Initial Interest Date" with respect to any series of Securities means the date of the Stated Maturity for the initial installment of interest on Securities of such series.

"Lease" means any Lease identified in a Schedule to a Series Supplemental Indenture, as such Lease may be amended from time to time pursuant to the applicable provisions thereof; "Leases" means each and every Lease.

"Lease Indenture" means any Lease Indenture identified in a Schedule to a Series Supplemental Indenture, as such Lease Indenture may be amended or supplemented from time to time pursuant to the applicable provisions thereof; "Lease Indentures" means each and every Lease Indenture.

"Lease Indenture Trustee" means the Lease Indenture Trustee identified in a Schedule to a Series Supplemental Indenture, until a successor Lease Indenture Trustee shall have become such pursuant to the applicable provisions of the Lease Indenture to which such Lease Indenture Trustee is a party, and thereafter "Lease Indenture Trustee" means the successor Lease Indenture Trustee; "Lease Indenture Trustees" means each and every Lease Indenture Trustee.

"Lease Payments" with respect to any Lease shall mean amounts payable under such lease in respect of (i) interim rent (if any), (ii) basic rent, (iii) casualty value, (iv) special casualty value, (v) extraordinary casualty value or (vi) any other amounts payable in connection with termination of such Lease, in each case as more fully described in and assigned pursuant to the related Lease Indenture; "Lease Payments" with respect to all Leases means the aggregate of Lease Payments under any and all Leases.

"Lessee Request" and "Lessee Order" mean, respectively, a written request and a written order signed in the name of APS by its President or one of its Vice Presidents or Assistant Vice Presidents and by its Treasurer or Secretary or one of its Assistant Treasurers or Assistant Secretaries or Associate Secretaries, or by any authorized agent of APS, and delivered to the Trustee.

"Lessor" or "Owner Trustee" means any Lessor or Owner Trustee identified in a Schedule to a Series Supplemental Indenture, until a successor shall have become such pursuant to the applicable provisions of the related Trust Agreement identified in said Schedule, and thereafter "Lessor" or "Owner Trustee" means such successor; "Lessors" or "Owner Trustees" means each and every Lessor or Owner Trustee.

"*Lessor Note*" means any promissory note issued by a Lessor under a Lease Indenture.

"*Lien of this Indenture*" or "*lien hereof*" means the lien and security interest created by these presents, or created by any concurrent or subsequent conveyance to the Trustee (whether made by the Company or any other Person and whether pursuant to a Series Supplemental Indenture or otherwise), or otherwise created, constituting any property a part of the Pledged Property held by the Trustee for the benefit of the Securities Outstanding hereunder.

"*Obligor*", when used with reference to the Securities or this Indenture, means APS and any successor to the obligations of APS under a Lease, and does not include the Trustee, the Lease Indenture Trustee, an Owner Trustee or an Equity Participant so long as they have not assumed such obligations; *provided, however*, that no reference to APS as an Obligor herein shall be construed as implying any guaranty by APS of the Securities.

"*Officers' Certificate*" means a certificate signed by the President or a Vice President, and by the Treasurer, the Secretary, or one of the Assistant Treasurers or Assistant Secretaries or Associate Secretaries, of APS, any Lessor or the Company, as the case may be, and delivered to the Trustee.

"*Opinion of Counsel*" means a written opinion of counsel for any Person either expressly referred to herein or otherwise satisfactory to the Trustee which may include, without limitation, counsel to the Company, any Lessor, the Lease Indenture Trustee, any Equity Participant or APS, whether or not such counsel is an employee of any of them.

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

(i) Securities theretofore cancelled by the Trustee or delivered to the Trustee for cancellation;

(ii) Securities for whose payment or redemption money in the necessary amount has been theretofore deposited with the Trustee in trust for the Holders of such Securities as provided in Section 12.01, provided that, if such Securities are to be redeemed (otherwise than through the operation of the Sinking Fund), notice of such redemption

has been duly given pursuant to this Indenture or provision therefor satisfactory to the Trustee has been made; and

(iii) Securities paid in full or in exchange for or in lieu of which other Securities have been authenticated and delivered pursuant to this Indenture unless held by a Holder in whose hands such Securities constitute valid obligations of the Company;

provided, however, that in determining whether the Holders of the requisite principal amount of Securities Outstanding have given any request, demand, authorization, direction, notice, consent or waiver hereunder, Securities owned by the Company or owned by APS or any Affiliate of the Company or of APS shall be disregarded and deemed not to be Outstanding, unless such Persons own 100% of the Securities owned by all Persons, except that, in determining whether the Trustee shall be protected in relying upon any such request, demand, authorization, direction, notice, consent or waiver, only Securities which the Trustee knows to be so owned shall be so disregarded. Securities so owned which have been pledged in good faith may be regarded as Outstanding if the pledgee establishes to the satisfaction of the Trustee the pledgee's right so to act with respect to such Securities and that the pledgee is not the Company or APS, or any Affiliate of the Company or of APS.

"Participation Agreement" means any Participation Agreement or other similar Lessor Note purchase document to which the Company is a party identified in a Schedule to a Series Supplemental Indenture, as such Participation Agreement or other purchase document may be amended from time to time pursuant to the applicable provisions thereof; "Participation Agreements" means each and every Participation Agreement.

"Paying Agent" means any Person acting as Paying Agent hereunder pursuant to Section 9.14.

"Paying Agent's Office" shall mean that office of the Paying Agent designated in Section 5.02.

"Permitted Investment" means (i) direct obligations of the United States of America, or (ii) obligations fully guaranteed by the United States of America, or (iii) certificates of deposit issued by, or bankers' accept-

ances of, or time deposits with, any bank, trust company or national banking association incorporated or doing business under the laws of the United States of America or one of the States thereof (but not exceeding \$15,000,000 in principal amount of all certificates of deposit and time deposits at any given time for any one bank, trust company or national banking association) having a combined capital and surplus of at least \$300,000,000 (including the Trustee, any Lease Indenture Trustee, any Lessor and any Paying Agent if such conditions are met), or (iv) commercial paper of companies incorporated or doing business under the laws of the United States of America or one of the States thereof (but not exceeding \$15,000,000 in principal amount at any given time for any one company) and in each case having a rating assigned to such commercial paper by Standard & Poor's Corporation or Moody's Investors Service, Inc. (or, if neither such organization shall rate such commercial paper at any time, by any nationally recognized rating organization in the United States of America) equal to the highest rating assigned by such organization, or (v) repurchase agreements fully collateralized by an obligation of the type described in clause (i) or (iv) above, pursuant to which a bank, trust company or national banking association referred to in clause (iii) above or another financial institution having a net worth of at least \$200,000,000 is obligated to repurchase any such obligation not later than 90 days after the purchase of any such obligation.

"Person" means any individual, corporation, partnership, joint venture, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

"Place of Payment", when used with respect to the Securities of any series, means the office or agency maintained pursuant to Section 5.02 and such other place or places, if any, where the principal of (and premium, if any) and interest on the Securities of that series are payable as specified in the Series Supplemental Indenture setting forth the terms of the Securities of such series.

"Pledged Lessor Note" means any Lessor Note identified in a Schedule to a Series Supplemental Indenture, as such Lessor Note may be amended or supplemented from time to time pursuant to the applicable provisions thereof, of the related Lease Indenture and of this Indenture; *"Pledged Lessor Notes"* means each and every Pledged Lessor Note.

"Pledged Property" has the meaning set forth in the Granting Clauses.

"Predecessor Securities" 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 2.09 in lieu of a lost, destroyed or stolen Security shall be deemed to evidence the same debt as the lost, destroyed or stolen Security.

"Principal Instruments" means the Pledged Lessor Notes, the Lease Indentures, the Participation Agreements and the Leases.

"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 (inclusive of accrued interest) at which it is to be redeemed pursuant to this Indenture and the terms of such Security.

"Regular Record Date" for the Stated Maturity of any installment of interest means the 15th. day (whether or not a Business Day) next preceding such Stated Maturity.

"Responsible Officer" when used with respect to the Trustee means any officer of the Trustee customarily performing corporate trust functions.

"Security Register" has the meaning specified in Section 2.08.

"Security Registrar" means any Person acting as Security Registrar hereunder pursuant to Section 9.14.

"Series Supplemental Indenture" means an indenture supplemental to this Indenture, for the purpose of specifying, in accordance with Article Two hereof, the form of the Securities of any series, and/or for the purpose of subjecting to the Lien of this Indenture the Pledged Lessor Notes related to such series; *"Series Supplemental Indentures"* means each and every Series Supplemental Indenture.

"Sinking Fund" has the meaning specified in Section 7.01.

"Special Record Date" for the payment of any defaulted interest means a date fixed by the Trustee pursuant to Section 2.10.

"Stated Maturity" when used with respect to any Security or any installment of interest thereon means the date specified in such Security as the fixed date on which the principal of such Security or such installment of interest is due and payable; except that when used with reference to a series of Securities which have maturities from their respective dates of issuance of one year or less, the Series Supplemental Indenture creating such series

may provide that the Stated Maturity of all Securities of such series shall be a stated date beyond such individual maturity dates.

"Trust Indenture Act" or "TIA" means the Trust Indenture Act of 1939 as in force at the date as of which this instrument was executed, except as provided in Section 11.06.

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

SECTION 1.02. *Compliance Certificates and Opinions.*

Upon any application or request by the Company, any Lessor or APS to the Trustee to take any action under any provision of this Indenture, the Company, such Lessor or APS, as the case may be, shall furnish to the Trustee an Officers' 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, *except* 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:

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

(2) 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;

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

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

SECTION 1.03. *Form of Documents Delivered to Trustee.*

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.

Any certificate or opinion of an officer of the Company, of any Lessor or of APS may be based, in so far as it relates to legal matters, upon a certificate or opinion of, or representations by, counsel, unless such officer knows that the certificate or opinion or representations with respect to the matters upon which his certificate or opinion is based are erroneous. Any such certificate or Opinion of Counsel may be based, in so far as it relates to factual matters, upon a certificate or opinion of, or representations by, an officer or officers of the Company, of any Lessor or of APS, as the case may be, stating that the information with respect to such factual matters is in the possession of the Company, such Lessor or APS, respectively, unless such counsel knows that the certificate or opinion or representations with respect to such matters are erroneous.

Any Opinion of Counsel stated to be based on the opinion of other counsel shall be accompanied by a copy of such other opinion.

Where any Person is required to make, give or execute two or more applications, requests, consents, certificates, statements, opinions or other instruments under this Indenture, they may, but need not, be consolidated and form one instrument.

SECTION 1.04. *Acts of Holders.*

(a) Any request, demand, authorization, direction, notice, consent, waiver or other action provided by this Indenture to be 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; and, except as herein otherwise expressly provided, such action shall become effective when such instrument or instruments are delivered to the Trustee and, where it is hereby expressly required, to the Company and to APS. Such instrument or instruments

(and the action embodied therein and evidenced thereby) are herein sometimes referred to as the "Act" of the Holders 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 Indenture and (subject to Section 9.01) conclusive in favor of the Trustee, the Company and APS, if made in the manner provided in this Section.

(b) The fact and date of the execution by any Person of any such instrument or writing may be proved by the certificate of any notary public or other officer of any jurisdiction authorized to take acknowledgments of deeds or administer oaths that the Person executing such instrument acknowledged to him the execution thereof, or by an affidavit of a witness to such execution sworn to before any such notary or other such officer and where such execution is by an officer of a corporation or association or a member of a partnership, on behalf of such corporation, association or partnership, 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 Trustee deems sufficient.

(c) The ownership of Securities shall be proved by the Security Register and the Trustee shall not be affected by notice to the contrary.

(d) Any request, demand, authorization, direction, notice, consent, waiver or other action by the Holder of any Security shall bind the Holder of every Security issued upon the transfer thereof or in exchange therefor or in lieu thereof, whether or not notation of such action is made upon such Security.

SECTION 1.05. *Notices, etc., to Trustee, APS and Company.*

Any request, demand, authorization, direction, notice, consent, 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,

(1) the Trustee by any Holder, by the Company, by APS or by an Authorized Agent shall be sufficient for every purpose hereunder if made, given, furnished or filed in writing to or with the Trustee at its Corporate Trust Office, or

(2) the Company by the Trustee, by any Holder, by APS or by an Authorized Agent shall be sufficient for every purpose hereunder if in writing and mailed, first-class postage prepaid, to the Company ad-

dressed to it at the address of its principal office specified in the first paragraph of this instrument or at any other address previously furnished in writing to the Trustee and APS by the Company for such purpose, or

(3) APS by the Trustee, by any Holder, by the Company or by an Authorized Agent shall be sufficient for every purpose hereunder if in writing and mailed, first-class postage prepaid, to APS addressed to it at the address of its principal office specified in the first paragraph of this instrument or at any other address previously furnished in writing to the Trustee and the Company by APS for such purpose.

SECTION 1.06. *Notices to Holders; Waiver.*

Where this Indenture provides for notice to Holders of any event, such notice shall be sufficiently given (unless otherwise herein expressly provided) if in writing and mailed, first-class postage prepaid, to each Holder, at his address 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. Where this Indenture provides for notice in any manner, such notice may be waived in writing by the Person entitled to receive such notice, either before or after the event, 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. 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, and any notice which is mailed in the manner herein provided shall be conclusively presumed to have been duly given.

SECTION 1.07. *Conflict with Trust Indenture Act.*

If any provision hereof limits, qualifies or conflicts with another provision hereof which is required to be included in this Indenture by any of the provisions of the TIA, such required provision shall control. Notwithstanding the foregoing, the provisions of the TIA contained in Sections 9.08, 9.13 and 10.03 shall not become operative under this Indenture until this Indenture shall have been qualified under the TIA.

SECTION 1.08. *Effect of Heading and Table of Contents.*

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

SECTION 1.09. *Successors and Assigns.*

All covenants, agreements, representations and warranties in this Indenture by the Trustee, APS and the Company shall bind and, to the extent permitted hereby, shall inure to the benefit of and be enforceable by their respective successors and assigns, whether so expressed or not.

SECTION 1.10. *Separability Clause.*

In case any provision in this Indenture or in the Securities 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 1.11. *Benefits of Indenture.*

Nothing in this Indenture or in the Securities, expressed or implied, shall give to any Person, other than the parties hereto and their successors hereunder, or the Holders of Securities as expressly provided herein, any benefit or any legal or equitable right, remedy or claim under this Indenture.

SECTION 1.12. *Governing Law.*

This Indenture and each Security are being executed and delivered in the State of New York, shall be deemed to be contracts made in such State and for all purposes shall be construed in accordance with and governed by the laws of the State of New York.

SECTION 1.13. *Legal Holidays.*

In any case where the Redemption Date or the Stated Maturity of any Security or of any installment of interest, or any date on which any defaulted interest is proposed to be paid, shall not be a Business Day, then (notwithstanding any other provision of this Indenture) payment of interest and/or principal (and premium, if any) need not be made on such date, but shall be made on the next succeeding Business Day with the same force and effect as if made on the Redemption Date or at the Stated Maturity, or

on the date on which the defaulted interest is proposed to be paid, and no interest in respect of such payment shall accrue for the period from and after such Redemption Date or Stated Maturity, or date for the payment of defaulted interest, as the case may be.

ARTICLE TWO

THE SECURITIES

SECTION 2.01. *Form of Security to Be Established by Series Supplemental Indenture.*

The Securities of each series shall be in the form (not inconsistent with this Indenture, including Section 2.05 hereof) as shall be established in one or more Series Supplemental Indentures.

SECTION 2.02. *Form of Trustee's Authentication.*

The Trustee's certificate of authentication on all Securities shall be in substantially the following form:

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

CHEMICAL BANK
as Trustee

By _____
Authorized Officer

SECTION 2.03. *Amount Unlimited; Issuable in Series; Limitations on Issuance.*

The aggregate principal amount of Securities which may be authenticated and delivered under this Indenture is unlimited. Securities may be issued hereunder up to the aggregate principal amount which may be authorized from time to time by the Board of Directors of the Company.

The terms of any series of Securities relative to payment of principal thereof, and premium (if any) and interest thereon, need not correspond exactly to the schedule for such payments under the related Pledged Lessor Notes.

The Securities may be issued in one or more series. There shall be established in one or more Series Supplemental Indentures, prior to the issuance of Securities of any series:

(1) the title of the Securities of the series (which shall distinguish the Securities of the series from all other Securities) and the form or forms of Securities of such series;

(2) any limit upon the aggregate principal amount of the Securities of such series that 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 2.07, 2.08, 2.09, 6.06 or 11.07);

(3) the date or dates on which the principal of the Securities of such series is payable;

(4) the rate or rates at which the Securities of such series shall bear interest, or the method by which such rate shall be determined, the date or dates from which such interest shall accrue, the interest payment dates on which such interest shall be payable and the record dates for the determination of Holders to whom interest is payable;

(5) the place or places where the principal of, and premium, if any and interest on, Securities of such series shall be payable (if other than as provided in Section 5.02);

(6) the price or prices at which, the period or periods within which and the terms and conditions upon which Securities of such series may be redeemed, in whole or in part, at the option of the Company, pursuant to any sinking fund or otherwise;

(7) the obligation, if any, of the Company to redeem, purchase or repay Securities of such series pursuant to any sinking fund or analogous provisions or at the option of a Holder thereof and the price or prices at which and the period or periods within which and the terms and conditions upon which Securities of the series shall be redeemed, purchased or repaid, in whole or in part, pursuant to such obligation;

(8) if other than denominations of \$1,000 and any multiple thereof, the denominations in which Securities of such series shall be issuable;

(9) any other terms of such series (which terms shall not be inconsistent with the provisions of this Indenture); and

(10) any trustees, authenticating or paying agents, warrant agents, transfer agents or registrars with respect to the Securities of such series;

provided, however, that, after giving effect to the issuance of a new series of the Securities and the subjection to the Lien of this Indenture of the related Pledged Lessor Notes, the average of the daily balance of Excess Funds for each fiscal year of the Company shall not exceed 10% of the average of the aggregate principal amount of Securities Outstanding on each day in such fiscal year. For purposes of the foregoing proviso, "Excess Funds" shall mean, for any day, amounts actually paid to the Trustee under the Pledged Lessor Notes in excess of amounts then due and payable in respect of Securities.

SECTION 2.04. *Authentication and Delivery of Securities.*

At any time and from time to time after the execution and delivery of this Indenture, the Company may deliver Securities of any series executed by the Company to the Trustee for authentication, together with a Company Order for the authentication and delivery of such Securities, and the Trustee shall thereupon authenticate and deliver such Securities in accordance with such Company Order, without any further action by the Company. No Security shall be secured by or 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, in the form provided for herein, executed by the Trustee by one of its Responsible Officers, and such certificate upon any Security shall be conclusive evidence, and the only evidence, that such Security has been duly authenticated and delivered hereunder. In authenticating such Securities and accepting the additional responsibilities under this Indenture in relation to such Securities, the Trustee shall be entitled to receive, and (subject to Section 9.01) shall be fully protected in relying upon:

(1) an executed Series Supplemental Indenture;

(2) an Officers' Certificate of the Company (a) certifying as to resolutions of the Board of Directors of the Company by or pursuant to which the terms of the Securities of such series were established, (b) certifying that all conditions precedent under this Indenture to the Trustee's authentication and delivery of such Securities have been complied with and (c) certifying that (x) the terms of the documents

referred to in clauses (3) and (4) below are not inconsistent with the terms of this Indenture as then and theretofore supplemented and (y) such documents comply with Exhibit A hereto (if applicable);

(3) fully executed counterparts (but not the original thereof) of (a) the Lease Indentures under which were issued the Pledged Lessor Notes relating to such series of Securities and (b) the Leases relating to such Pledged Lessor Notes;

(4) the originals of the Pledged Lessor Notes relating to such series of Securities in an aggregate principal amount equal to not less than the aggregate principal amount of such series of Securities proposed to be authenticated and delivered;

(5) signed copies, either addressed to the Trustee or accompanied by statements that the Trustee may rely on such documents, of all certificates and opinions of counsel delivered (i) to the Company in connection with its purchase pursuant to the applicable Participation Agreements of the Pledged Lessor Notes relating to such series of Securities (ii) to the Lease Indenture Trustee in connection with the issuance of such Pledged Lessor Notes and (iii) to the Lessor under the applicable Lease or Participation Agreement in connection with any Refunding Loan, Releveraging Loan or Supplemental Financing (as such terms are defined in such Participation Agreement) and, to the extent not covered by such opinions, Opinions of Counsel (x) to the effect that: (a) the form or forms and the terms of such Securities have been established by a Series Supplemental Indenture as permitted by Sections 2.01 and 2.03 in conformity with the provisions of this Indenture; (b) such Securities, when authenticated and delivered by the Trustee and issued by the Company in the manner and subject to any conditions specified in such Opinion of Counsel, will constitute valid and binding obligations of the Company, except to the extent that the enforcement thereof may be limited by applicable bankruptcy, insolvency, reorganization, moratorium and other similar laws now or hereafter in effect relating to creditors' rights generally; and (c) all laws and requirements in respect of the execution and delivery by the Company of the Securities have been complied with; and (y) covering such other matters as the Trustee may reasonably request;

(6) duly executed Extension Letters relating to the Pledged Lessor Notes; and

(7) in circumstances where the Pledged Lessor Notes relating to such series of Securities are executed and delivered for the purposes described in clause (ii) of paragraph (1) of Section 3.5 of any Lease Indenture, (A) a certificate of an independent public accountant acceptable to the Trustee (who shall not be an employee of the Company, APS or any Affiliate of either) to the effect that the principal amount of Securities to be authenticated does not exceed the total cost (including allowance for funds used during construction to the extent permitted by generally accepted accounting principles) of any Capital Improvement (as defined in such Lease Indenture) financed with the proceeds of such Pledged Lessor Notes and (B) a certificate of an engineer, appraiser or other expert acceptable to the Trustee (who may be an officer or employee of APS except as would be required by Section 314(d)(3) of the Trust Indenture Act of 1939, as amended) to the effect that the fair value of any Capital Improvement as of its respective date of incorporation or installation was not less than the total cost (including allowance for funds used during construction to the extent permitted by generally accepted accounting principles) of such Capital Improvement as of the date financed with the proceeds of such Pledged Lessor Notes;

provided, however, that if a series of Securities is to be authenticated by the Trustee in advance of the actual delivery to the Trustee of the Pledged Lessor Notes relating thereto, (x) the documents described in the foregoing clauses (2)(c), (3), (4), (5) (other than the opinion described in subclauses (x) and (y)), (6) and (7) need not be delivered in connection with such authentication, but shall be delivered in connection with the release of the proceeds of the sale of such series of Securities in accordance with Sections 2.15 and 13.01 hereof and (y) the form of the Series Supplemental Indenture shall be appropriately modified to reflect the later delivery and pledge of the related Pledged Lessor Notes.

Receipt by the Trustee of the Officer's Certificate referred to in clause (2) above shall be conclusively presumed for all purposes of this Indenture to establish that the Lease Indentures, the Leases and the Pledged Lessor Notes referred to in such certification comply with the requirements of Exhibit A hereto.

The Trustee shall have the right to decline to authenticate and deliver any Securities under this Section if the Trustee, being advised by counsel, determines that such action may not lawfully be taken by the Company or if

the Trustee in good faith by its board of directors or board of trustees, executive committee, or a trust committee of directors or trustees and/or responsible officers shall determine that such action would expose the Trustee to personal liability.

SECTION 2.05. *Form and Denominations.*

The Securities of each series shall be in registered form and may have such letters, numbers or other marks of identification and such legends or endorsements printed, lithographed or engraved thereon, as may be required to comply with the rules of any securities exchange or to conform to any usage in respect thereof, or as may, consistently herewith, be prescribed by the Board of Directors of the Company or by the officers executing such Securities, such determination by said officers to be evidenced by their signing the Securities.

The definitive Securities shall be printed, lithographed or engraved or produced by any combination of these methods on steel engraved borders or may be produced in any other manner permitted by the rules of any securities exchange, all as determined by the officers executing such Securities, as evidenced by their execution of such Securities.

All Securities of any one series shall be substantially identical except as to denomination and Stated Maturity and except as may otherwise be provided herein or in the Series Supplemental Indenture setting forth the terms of the Securities of such series.

The Securities are issuable only in denominations of \$1,000 and/or any integral multiple thereof.

SECTION 2.06. *Execution of Securities.*

The Securities shall be executed on behalf of the Company by its President or one of its Vice Presidents under its corporate seal reproduced thereon and attested by its Secretary or one of its Assistant Secretaries. The signature of any such officers on the Securities may be manual or facsimile.

Securities bearing the manual or facsimile signatures of individuals who were at the time such signatures were affixed the proper officers of the Company shall bind the Company, notwithstanding that such individuals or any of them have ceased to hold such offices prior to the authentication and delivery of such Securities or did not hold such offices at the date of such Securities.

SECTION 2.07. *Temporary Securities.*

Pending the preparation of definitive Securities of any series, the Company may execute, and upon Company Order the Trustee shall authenticate and deliver, temporary Securities of such series which are printed, lithographed, typewritten, photocopied or otherwise produced, in any denomination, substantially of the tenor of the definitive Securities in lieu of which they are issued and 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.

If temporary Securities of any series are issued, the Company will cause definitive Securities of such series to be prepared without unreasonable delay. After the preparation of definitive Securities of such series, the temporary Securities of such series shall be exchangeable for definitive Securities of such series upon surrender of the temporary Securities of such series at the office or agency of the Company, for such purpose, in the Place of Payment, without charge to the Holder. Upon surrender for cancellation of any one or more temporary Securities of any series the Company shall execute and the Trustee shall authenticate and deliver in exchange therefor a like aggregate principal amount of definitive Securities of such series of authorized denominations. Until so exchanged such temporary Securities of any series shall in all respects be entitled to the same benefits under this Indenture as definitive Securities of such series.

SECTION 2.08. *Registration, Transfer and Exchange.*

The Trustee shall cause to be kept at the Corporate Trust Office a register in which, subject to such reasonable regulations as the Company may prescribe, the Company shall provide for the registration of Securities and of registration of transfers and exchanges of Securities. This register and, if there shall be more than one Security Registrar, the combined registers maintained by all such Security Registrars, are herein sometimes referred to as the "*Security Register*".

Upon surrender for registration of transfer of any Security of any series at the Corporate Trust Office, or at any office or agency maintained for such purpose pursuant to Section 9.14(a), 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 of the same Stated Maturity for principal and interest and of a like aggregate principal amount.

At the option of the Holders, Securities of any series may be exchanged for an equal aggregate principal amount of Securities of the same series and of the same Stated Maturity for principal and interest and of any authorized denominations, upon surrender of the Securities to be exchanged at the Corporate Trust Office, or at any office or agency maintained for such purpose pursuant to Section 9.14(a). Whenever any Securities are so surrendered for exchange, the Company shall execute, and the Trustee or a duly authorized authenticating agent shall authenticate and deliver, the Securities which the Securityholder making the exchange is entitled to receive.

All Securities issued upon any transfer or exchange of Securities shall be the valid obligations of the Company, evidencing the same debt, and entitled to the same security and benefits under this Indenture, as the Securities surrendered upon such transfer or exchange.

Every Security presented or surrendered for registration of transfer or exchange shall be duly endorsed, or be accompanied by a written instrument of transfer in form satisfactory to the Security Registrar duly executed, by the Holder thereof or his attorney duly authorized in writing.

No service charge shall be required of any Securityholders participating in any transfer or exchange of Securities in respect of such transfer or exchange, but the Security Registrar may require payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in connection with any transfer or exchange of Securities, other than exchanges pursuant to Sections 2.07, 6.06 or 11.07 not involving any transfer.

The Security Registrar shall not be required (i) to issue, transfer or exchange any Security of any series during a period beginning at the opening of business 15 days before the day of the mailing of a notice of redemption of Securities of such series selected for redemption under Section 6.02 or 7.02 and ending at the close of business on the day of such mailing, or (ii) to transfer or exchange any Security so selected for redemption in whole or in part except the unredeemed portion of any Security selected for redemption in part.

SECTION 2.09. *Mutilated, Destroyed, Lost and Stolen Securities.*

If (i) any mutilated Security is surrendered to the Trustee, or the Company, APS, the Security Registrar and the Trustee receive evidence to

their satisfaction of the destruction, loss or theft of any Security, and (ii) there is delivered to the Company, to APS, to the Security Registrar and to the Trustee evidence to their satisfaction of the ownership and authenticity thereof, and such security or indemnity as may be required by them to save each of them harmless, then, in the absence of notice to the Company, to APS, to the Security Registrar or to the Trustee that such Security has been acquired by a bona fide purchaser, the Company shall execute and upon its request the Trustee shall authenticate and deliver, in exchange for or in lieu of any such mutilated, destroyed, lost or stolen Security, a new Security of like tenor and principal amount, bearing a number not contemporaneously outstanding.

In case any such mutilated, destroyed, lost or stolen Security has become or is about to become due and payable, the Company may, upon satisfaction of the conditions set forth in clauses (i) and (ii) of the preceding paragraph, instead of issuing a new Security, pay such Security.

Upon the issuance of any new Security under this Section, the Security Registrar 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 expenses connected therewith.

Every new Security 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, and shall be entitled to all the security and benefits of this Indenture equally and proportionately with any and all other Securities 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 2.10. *Payment of Interest; Interest Rights Preserved.*

Interest on any Security which is payable, and is punctually paid or duly provided for, at any Stated Maturity of an installment of interest 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. At the option of the Company, payment of interest on any Security may be made by check mailed to the address of the Person entitled thereto as such address shall appear in the

Security Register or in such other manner as shall be established in a Series Supplemental Indenture creating the series of which such Security is a part.

Any interest on any Security of any series which is payable, but is not punctually paid or duly provided for, at any Stated Maturity of an installment of interest shall forthwith cease to be payable to the Holder on the relevant Regular Record Date by virtue of having been such Holder; and such defaulted interest may be paid by the Company, at its election in each case, as provided in paragraph (1) or paragraph (2) below:

(1) The Company may elect, which election shall be at the direction of any Lessor whose Pledged Lessor Note is in default in respect of the payment of interest and who is proposing to make payment of all or part of such defaulted interest, to make payment of any defaulted interest to the Persons in whose names the Securities of such series in respect of which interest is in default (or their respective Predecessor Securities) are registered at the close of business on a Special Record Date for the payment of such defaulted interest, which shall be fixed in the following manner. Such Lessor shall notify the Trustee and the Paying Agent in writing of the amount of defaulted interest proposed to be paid on each such Security and the date of the proposed payment, and at the same time there shall be deposited with the Trustee an amount of money equal to the aggregate amount proposed to be paid in respect of such defaulted interest or there shall be made 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 defaulted interest as in this paragraph provided. Thereupon the Trustee shall fix a Special Record Date for the payment of such defaulted interest which shall be not more than 15 nor less than 10 days prior to the date of the proposed payment and not less than 10 days after the receipt by the Trustee of the notice of the proposed payment. The Trustee shall promptly notify the Company, APS and the Security Registrar of such Special Record Date and, in the name and at the expense of the Company, shall cause notice of the proposed payment of such defaulted interest and the Special Record Date therefor to be mailed, first class postage prepaid, to each holder of a Security of such series at his address as it appears in the Security Register, not less than 10 days prior to such Special Record Date. Notice of the proposed payment of such defaulted interest and the Special Record Date therefor having been mailed as

aforesaid, such defaulted interest shall be paid to the Persons in whose names the Securities of such series (or their respective Predecessor Securities) are registered on such Special Record Date and shall no longer be payable pursuant to the following paragraph (2).

(2) The Company may make, or cause to be made, payment of any defaulted interest in any other lawful manner not inconsistent with the requirements of any securities exchange on which the Securities in respect of which interest is in default 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 paragraph, such payment shall be deemed practicable by the Trustee.

Subject to the foregoing provisions of this Section, each Security delivered under this Indenture upon 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, and each such Security shall bear interest from whatever date shall be necessary so that neither gain nor loss in interest shall result from such transfer, exchange or replacement.

SECTION 2.11. *Persons Deemed Owners.*

Prior to due presentment for registration of transfer, the Person in whose name any Security is registered shall be deemed to be the owner of such Security for the purpose of receiving payment of principal of (and premium, if any), and (subject to Section 2.10) interest on, such Security and for all other purposes whatsoever, whether or not such Security be overdue, regardless of any notice to anyone to the contrary.

SECTION 2.12. *Cancellation.*

All Securities surrendered for payment, redemption, credit against any Sinking Fund payment or redemption payment, transfer or exchange shall, if surrendered to any Person other than the Trustee, be delivered to the Trustee for cancellation. The Company may at any time deliver to the Trustee for cancellation any Securities previously authenticated and delivered hereunder which the Company may have acquired in any manner whatsoever, and all Securities so delivered shall be promptly cancelled by the Trustee. No Securities shall be authenticated in lieu of or in exchange for any Securities cancelled as provided in this Section, except as expressly

permitted by this Indenture. All cancelled Securities held by the Trustee shall be destroyed and certification of their destruction delivered to the Company unless, by Company Request, the Company otherwise directs.

SECTION 2.13. *Dating of Securities; Authentication.*

Except as otherwise provided in the Series Supplemental Indenture creating a series of Securities, each Security of any series shall be dated the date of the original issuance of the Securities of such series by the Company, which date shall be specified by the Company in the Company Order delivered to the Trustee pursuant to Section 2.04 in connection with the original authentication and delivery of the Securities of such series.

SECTION 2.14. *Source of Payments; Rights and Liabilities of Lessors and Equity Participants.*

Except as otherwise specifically provided in this Indenture, all payments of principal and premium (if any) and interest to be made by the Trustee in respect of the Securities or under this Indenture shall be made only from Pledged Property or the income and proceeds received by the Trustee therefrom. Each Holder, by its acceptance of a Security, agrees that (x) it will look solely to the Pledged Property or the income and proceeds received by the Trustee therefrom to the extent available for distribution to such Holder as herein provided and (y) none of any Equity Participant, any Lessor, any Lease Indenture Trustee or the Trustee is liable to any Holder or, in the case of any Equity Participant, Lessor and Lease Indenture Trustee, to the Trustee for any amounts payable under any Security or, except as provided herein with respect to the Trustee, for any liability under this Indenture. An Equity Participant, Lessor or Lease Indenture Trustee shall not have any duty or responsibility under this Indenture or the Securities to any Holder or to the Trustee.

SECTION 2.15. *Sale of Securities; and Application of Proceeds from the Sale of Securities.*

(a) Promptly upon receipt by the Company of the proceeds from any sale of a series of the Securities, the Company shall deposit such proceeds with the Trustee. The funds so deposited shall be held by the Trustee in a separate account as part of the Pledged Property and shall be invested, applied and distributed by the Trustee as provided herein.

(b) Subject to the provisions of Section 13.01, upon the issuance of the Pledged Lessor Notes related to any series of Securities and the delivery thereof to the Trustee to be subjected to the Lien of this Indenture pursuant to a Series Supplemental Indenture, the Trustee shall pay to the Lessor obligated in respect of any such Pledged Lessor Note, out of funds held by the Trustee in such separate account as Pledged Property, an amount equal to the principal amount of such Pledged Lessor Note in respect of which such Lessor is obligated. All payments to be made by the Trustee to any Lessor shall be made in immediately available funds at the respective offices designated by such Lessor.

ARTICLE THREE

PROVISIONS AS TO PLEDGED PROPERTY

SECTION 3.01. *Holding of Pledged Securities.*

The Trustee is authorized in its discretion to cause to be registered in its name, as Trustee, or in the name of its nominee, any and all coupon bonds which it may receive as part of the Pledged Property, or it may cause the same to be exchanged for registered bonds without coupons of any denomination. The Trustee may cause to be transferred into its name, as Trustee, or into the name of its nominee, any and all registered bonds which it may receive as part of the Pledged Property, or may cause such registered bonds to be exchanged for coupon bonds. All Pledged Lessor Notes assigned to and pledged with the Trustee pursuant to any provision of this Indenture or any Series Supplemental Indenture shall be endorsed in blank for transfer or be accompanied by proper instruments of assignment satisfactory to the Trustee, duly executed by the Company. The Company will deliver promptly to the Trustee such documents, certificates and opinions as the Trustee may reasonably request in connection with subjection of any securities to the Lien of this Indenture to the extent contemplated hereby.

SECTION 3.02. *Disposition of Payments on Pledged Property.*

Unless and until all Outstanding Securities have been paid in full or provision for the payment of such Securities has been made in accordance with this Indenture, the Trustee shall be entitled to receive all principal, premium (if any) and interest paid in respect of any Pledged Lessor Notes and interest paid on bonds or other obligations or indebtedness which may

be subject to the lien of this Indenture and shall apply the same to the payment of the principal of, and premium (if any) and interest on, the Securities when and as they become due and payable pursuant to, and in accordance with, this Indenture. The Trustee shall duly note on the Schedules attached to the Pledged Lessor Notes or by other appropriate means all payments of principal, premium, if any, and interest made on the Pledged Lessor Notes.

SECTION 3.03. *Exercise of Rights and Powers Under Pledged Lessor Notes and Lease Indentures.*

The Trustee shall not take any action as the holder of the Pledged Lessor Notes to direct any Lease Indenture Trustee in any respect or to vote any Pledged Lessor Note or any portion thereof except as specified in this Section. The Trustee shall give notice to the Securityholders of the occurrence of any event of default or default under any Lease Indenture, and of every Event of Loss or Deemed Loss Event occurring under a Lease, but only to the extent the same shall actually be known by an officer in the corporate trustee administration department of the Trustee. The Trustee may, at any time, and shall, upon the request of any Lease Indenture Trustee made to the Trustee to give any direction or to vote its interest in the Pledged Lessor Notes, request from Securityholders directions as to (i) whether or not to direct such Lease Indenture Trustee to take or refrain from taking any action which holders of a Pledged Lessor Note have the option to direct and (ii) how to vote any Pledged Lessor Note if a vote has been called for with respect thereto. In addition, any Securityholder may at any time request the Trustee to direct, or to participate in the direction of, any action under any Lease Indenture to the extent that the Trustee may do so under such Lease Indenture. Upon receiving from Securityholders any directions as to the taking or the refraining from taking, of any action, or the voting of any Pledged Lessor Note, the Trustee shall specify to the Lease Indenture Trustee the principal amount of the Pledged Lessor Note which is in favor of the action or vote, the principal amount of the Pledged Lessor Note which is opposed to the action or vote, and the principal amount of the Pledged Lessor Note which is not taking any position for the action or vote. Such principal amounts shall be determined by allocating the total principal amount of the Pledged Lessor Notes with respect to which direction is to be given the proportionate principal amount of Securities taking corresponding positions or not taking any position, based on the aggregate principal amount of Securities Outstanding. In addition, the

Trustee shall certify to the Lease Indenture Trustee that the principal amounts of Securities taking such corresponding positions or not taking any position was determined in accordance with the provisions of this Indenture.

SECTION 3.04. *Certain Actions in Case of Judicial Proceedings.*

In case all or any part of the property of any Lessor or any other Person which may be deemed an obligor in respect of the Pledged Lessor Notes shall be sold at any judicial or other involuntary sale, the Trustee shall receive any portion of the proceeds of such sale accruing on the Pledged Property held hereunder, and such proceeds shall be held as provided in Section 3.05.

SECTION 3.05. *Cash Held by Trustee Treated as a Deposit.*

Any and all cash held by the Trustee under any provision of this Indenture may be treated by the Trustee, until required to be paid out hereunder, as a deposit, in trust, without any liability for interest.

ARTICLE FOUR

WITHDRAWAL OF COLLATERAL.

SECTION 4.01. *Withdrawal of Collateral.*

Except as provided in Section 4.02 and Article Thirteen, none of the Pledged Property shall be subject to withdrawal unless and until all Outstanding Securities have been paid in full or provision for such payment has been made in accordance with the terms of this Indenture and the Trustee shall have received the documents and opinions required by Section 4.02 or Article Twelve.

SECTION 4.02. *Reassignment of Pledged Lessor Notes upon Payment.*

Upon receipt of payment in full of the principal of; and premium (if any) and interest on, any Pledged Lessor Note held by the Trustee, the Trustee shall deliver to the Company said Pledged Lessor Note and any instrument of transfer or assignment necessary to reassign to the Company said Pledged Lessor Note and the interest of the Company (if any) in the Lease Indenture relating thereto; provided that nothing herein contained shall prevent the Trustee from presenting any Pledged Lessor Note to a Lease Indenture Trustee for final payment in accordance with the applicable provisions of the related Lease Indenture.

ARTICLE FIVE

COVENANTS

SECTION 5.01. *Payment of Principal, Premium (if any) and Interest.*

The Company will duly and punctually pay, or cause to be paid, the principal of, and premium, if any, and interest on, the Securities in accordance with the terms of the Securities and this Indenture.

SECTION 5.02. *Maintenance of Office or Agency.*

The Company will maintain in the Borough of Manhattan, The City of New York, an office or agency where Securities may be presented or surrendered for payment, where Securities may be surrendered for transfer or exchange and where notices and demands to or upon the Company in respect of Securities and this Indenture may be served. The Paying Agent's Office is hereby designated as such office or agency. APS will give prompt written notice to the Trustee of the location, and of any change in the location, of each such office or agency. If at any time the Company shall fail to maintain any such office or agency or the Company or APS shall fail to furnish the Trustee with the address thereof, such presentations, surrenders, notices and demands may be made or served at the Corporate Trust Office of the Trustee, and the Company hereby appoints the Trustee its agent to receive all such presentations, surrenders, notices and demands.

SECTION 5.03. *Money for Security Payments to be Held in Trust.*

All moneys deposited with the Trustee or with any Paying Agent for the purpose of paying the principal of or premium, if any, or interest on Securities shall be deposited and held in trust for the benefit of the Holders of the Securities entitled to such principal, premium, if any, or interest, subject to the provisions of this Section. Moneys so deposited and held in trust shall not be a part of the Pledged Property but shall constitute a separate trust fund for the benefit of the Holders of the relevant Securities.

The Company may at any time, for the purpose of obtaining the satisfaction and discharge of this Indenture or for any other purpose, pay, or direct any Paying Agent to pay, to the Trustee all sums held in trust by such Paying Agent, such sums to be held by the Trustee upon the same trusts as those upon which such sums were held by such Paying Agent; 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 in trust for the payment of the principal of or premium, if any, or interest on any Security and remaining unclaimed for three years (or such lesser period as may be required by law to give effect to this provision) after such principal, premium or interest has become due and payable shall be paid to the Company on Company Request (to the extent such monies shall have been deposited by the Company) or to any other Person on its request (to the extent such monies shall have been deposited by such other Person); and the Holder of such Security shall thereafter, as an unsecured general creditor, look only to the Company or such other Person, to the extent such monies shall have been paid to the Company or such other Person, as the case may be, for payment thereof, and all liability of the Trustee or such Paying Agent with respect to such trust money shall thereupon cease; *provided, however*, that the Trustee or such Paying Agent, before being required to make any such repayment, may at the expense of the Company or, to the extent such monies are to be paid to another Person, such other Person cause to be mailed to each such Holder notice that such money remains unclaimed and that, after a date specified therein, which shall not be less than 30 days from the date of such mailing, any unclaimed balance of such money then remaining will be repaid to the Company or such other Person.

SECTION 5.04. *Maintenance of Corporate Existence.*

The Company, at its own cost and expense, will do or cause to be done all things necessary to preserve and keep in full force and effect its corporate existence, rights and franchises, except as otherwise specifically permitted in this Indenture; *provided, however*, that the Company shall not be required to preserve any right or franchise if the Board of Directors of the Company shall determine that the preservation thereof is no longer desirable in the conduct of the business of the Company and that the loss thereof is not disadvantageous in any material respect to the Securityholders.

SECTION 5.05. *Protection of Pledged Property.*

The Company and APS will from time to time execute and deliver all such supplements and amendments hereto and all such financing statements, continuation statements, instruments of further assurance, and other instruments necessary to

(i) grant more effectively all or any portion of the Pledged Property,

(ii) maintain or preserve the lien of this Indenture, or carry out more effectively the purposes hereof,

(iii) perfect, publish notice of, or protect the validity of, any grant made or to be made by this Indenture,

(iv) enforce any of the Securities, or

(v) preserve and defend title to any Securities or other instrument included in the Pledged Property and the rights of the Trustee, and of the Securityholders, in such Securities or other instrument against the claims of all persons and parties.

The Company and APS hereby designate the Trustee its agent and attorney-in-fact to execute any financing statement, continuation statement or other instrument required pursuant to this Section.

SECTION 5.06. *Opinions as to Pledged Property.*

Promptly after the execution and delivery of this Indenture and of each Series Supplemental Indenture or other supplemental indenture or other instrument of further assurance, the Company shall furnish to the Trustee an Opinion of Counsel stating that, in the opinion of such Counsel, this Indenture and all such Series Supplemental Indentures, other supplemental indentures and other instruments of further assurance have been properly recorded, registered and filed to the extent necessary to make effective the lien intended to be created by this Indenture, and reciting the details of such action or referring to prior Opinions of Counsel in which such details are given, and stating that all financing statements and continuation statements have been executed and filed that are necessary fully to preserve and protect the rights of the Securityholders and the Trustee, or stating that, in the opinion of such Counsel, no such action is necessary to make such lien effective.

On or before May 1, in each calendar year, beginning with the first calendar year commencing more than three months after the date of authentication and delivery of any Securities, the Company shall furnish to the Trustee an Opinion of Counsel either stating that, in the opinion of such counsel, such action has been taken with respect to the recording, filing, re-recording and re-filing of this Indenture, any Series Supplemental Inden-

ture and any other requisite documents and with respect to the execution and filing of any financing statements and continuation statements as is necessary to maintain the lien and security interest created by this Indenture with respect to the Pledged Property and reciting the details of such action or stating that in the opinion of such counsel no such action is necessary to maintain such lien and security interest. Such Opinion of Counsel shall also describe the recording, filing, re-recording and re-filing of this Indenture, any Series Supplemental Indenture and any other requisite documents and the execution and filing of any financing statements and continuation statements that will, in the opinion of such counsel, be required to maintain the lien and security interest of this Indenture with respect to the Pledged Property until May 1 in the following calendar year.

SECTION 5.07. *Performance of Obligations*

(a) Neither the Company nor APS will take any action or permit any action to be taken by others which would release any Person from any of such Person's covenants or obligations under any instrument included in the Pledged Property, or which would result in the amendment, hypothecation, subordination, termination or discharge of, or impair the validity or effectiveness of, any such instrument, except as expressly provided in this Indenture or such instrument.

(b) APS will fully perform all of its obligations under the Leases.

SECTION 5.08. *Negative Covenants.*

During such time as any Security issued hereunder is Outstanding, the Company will not:

(i) sell, transfer, exchange or otherwise dispose of any portion of the Pledged Property except as expressly permitted by this Indenture;

(ii) engage in any business or activity other than in connection with, or relating to, the issuance of Securities pursuant to this Indenture and application of the proceeds thereof as herein provided, or amend Article Third, Fourth or Sixth of its Certificate of Incorporation as in effect on the date of execution and delivery of this Indenture, without, in each case, the consent of the Holders of not less than 66⅔% of the aggregate principal amount of the Securities then Outstanding; notwithstanding the foregoing, however, the Company may, with respect to one or more series of Securities (or one or more Stated Maturities within any series), enter into credit or liquidity support

facilities (including, but without limitation, bank letters of credit, bank lines of credit and bonds of insurance);

(iii) issue bonds, notes or other evidences of indebtedness other than (A) Securities issued hereunder or (B) bonds, notes or other evidences of indebtedness permitted by clause (ii) above;

(iv) incur, assume or guaranty any indebtedness of any Person;

(v) dissolve or liquidate in whole or in part;

(vi) take any action which would (1) permit the validity or effectiveness of this Indenture or any grant of any of the Pledged Property to be impaired, or permit the Lien of this Indenture to be amended, hypothecated, subordinated, terminated or discharged, or permit any Person to be released from any covenant or obligation under this Indenture, (2) permit any lien, charge, security, mortgage or other encumbrance (other than the Lien of this Indenture) to be created on or extend to or otherwise arise upon or burden the Pledged Property or any part thereof or any interest therein or the proceeds thereof, or (3) permit the Lien of this Indenture not to constitute a valid first priority security interest in the Pledged Property; or

(vii) institute any proceedings to be adjudicated a bankrupt or insolvent, or consent to the institution of bankruptcy or insolvency proceedings against it, or file a petition or answer or consent seeking reorganization or relief under the Federal Bankruptcy Code or any other applicable federal or state law or law of the District of Columbia, or consent to the filing of any such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company or any substantial part of its property, or make an assignment for the benefit of its creditors, or admit in writing its inability to pay its debts generally as they become due, or take any corporate action in furtherance of the foregoing.

SECTION 5.09. *Administration of Principal Instruments.*

(a) Without the consent of the Holders of a majority in principal amount of Outstanding Securities, the Trustee shall not consent to any Change in any Principal Instrument; *provided, however,* that the Trustee may consent to any Change in any Principal Instrument if such Change is permitted by subsection (b) of this Section 5.09.

(b) Subject to the provisions of subsection (c) of this Section 5.09, the Trustee may consent to any Change in any Principal Instrument (it being understood that Changes in Principal Instruments other than the Pledged Lessor Notes do not require the Trustee's consent except to the extent that such requirement arises from the fact that the Trustee is a Holder of Pledged Lessor Notes) if such Change is:

(1) to cure any ambiguity, to correct or supplement any provision in such Principal Instrument which may be defective or inconsistent with any other provision in such Principal Instrument or any related Principal Instrument, or to make any other provisions with respect to matters arising under any such Principal Instrument, provided, in each instance, that such action shall not materially adversely affect the interests of Holders of Securities; or

(2) to add to the covenants and agreements of the parties to such Principal Instrument other covenants and agreements thereafter to be observed by any such party, or to surrender any right or power therein reserved to or conferred upon the Company; or

(3) to amend or supplement such Principal Instrument, or to give any consent or grant any waiver thereunder, so long as thereafter such Principal Instrument will comply with the requirements (if any) of Exhibit A hereto; *provided* that such action does not materially adversely affect the interests of Holders of Securities; or

(4) in any other manner not inconsistent with Exhibit A hereto; *provided* that such action does not materially adversely affect the interests of Holders of Securities; or

(5) a Change in the Lease permitted by applicable provisions of the related Lease Indenture; or

(6) to describe more fully and to amplify or correct the description of any property or rights assigned or pledged by such Principal Instrument or intended so to be, or to assign, pledge, mortgage or grant a security interest in any additional property, rights and interests, subject to such liens, restrictions or other encumbrances, if any, as shall be therein specifically described; or

(7) in the case of a Lease Indenture, to enable the Lease Indenture Trustee thereunder to confer upon holders of Pledged Lessor Notes any additional rights, remedies, powers or authorities that may lawfully be granted or conferred upon such holders; or

(8) to evidence the appointment of a separate or co-Lease Indenture Trustee or the succession of a new Lease Indenture Trustee; or

(9) to evidence the succession of or assumption by a successor or assignee Lessee under the Leases and the Participation Agreements or to evidence the succession of a new Lessor or Owner Trustee under any Principal Instrument to which it is a party; or

(10) permitted by the terms of such Principal Instrument to be made without the consent of or notice to the holders of the related Pledged Lessor Notes; or

(11) to provide for the issuance of Lessor Notes in addition to the Pledged Lessor Notes relating to such Principal Instruments in accordance with the applicable provisions of the related Principal Instruments.

(c) The Trustee shall not consent to any Change with respect to a Principal Instrument, whether effected pursuant to subsection (a) or pursuant to subsection (b) of this Section 5.09, anything in such subsections or elsewhere in this Indenture to the contrary notwithstanding, without the consent of the Holder of each Outstanding Security affected thereby if such Change would:

(1) except as provided in any Lease, change such Lease in such a way as to change the timing or reduce the amount of any Lease Payment, or otherwise to release, except as provided in such Lease, APS from its obligation under such Lease in respect of payment of Lease Payments; or

(2) modify, amend or supplement the Participation Agreements in such a way as to, or give any consent, waiver, authorization or approval which would, release any Equity Participant from its payment obligations contained in said Participation Agreements.

(d) Except during the continuance of an Event of Default hereunder, upon request of the Company or APS, the Trustee shall consent to any Change permitted by this Section 5.09 which requires the Trustee's consent, and shall execute any instrument requested by the Company or APS, as the case may be, for the purpose of confirming such consent, but only upon receipt by the Trustee of an Officers' Certificate and an Opinion of Counsel of the Company or APS, as the case may be, each stating that such Change is authorized by this Indenture and that execution of such instrument is appropriate to confirm such consent, unless such Change adversely affects the Trustee's rights, duties or immunities under this Indenture or other-

wise, in which case the Trustee may, in its discretion, but shall not be obligated to, give such consent, and the Trustee shall be fully protected in relying on such Officers' Certificate and Opinion of Counsel.

SECTION 5.10. *Annual Statement as to Compliance.*

(a) APS and the Company each will deliver to the Trustee, on or before 120 days after the end of each of its fiscal years, a written statement (which need not comply with Section 1.02) signed by its President or one of its Vice Presidents and by its Treasurer or one of its Assistant Treasurers or its Comptroller or one of its Assistant Comptrollers, stating, as to each signer thereof, that

(1) a review of the activities of APS or the Company, as the case may be, required during such year of APS or the Company, as the case may be, under this Indenture has been made under their supervision; and

(2) to the best of their knowledge, based on such review, APS or the Company, as the case may be, has fulfilled all its obligations under this Indenture throughout such year, or, if there has been a default in the fulfillment of any such obligation, specifying each such default known to such officer and the nature and status thereof.

(b) APS and the Company each will deliver to the Trustee, promptly after having obtained knowledge thereof, written notice of any event which with the giving of notice or lapse of time, or both, would become an Event of Default under Section 8.01.

SECTION 5.11. *Delivery of Certificate of Independent Public Accountant.*

APS will cause to be delivered to the Trustee any certificate of an independent public accountant (who shall not be an employee of the Company, APS or any Affiliate of either) delivered to any Lease Indenture Trustee pursuant to Section 2.4(c) of any Lease Indenture.

SECTION 5.12. *Delivery of Certificate of Engineer, Appraiser or Other Expert.*

In connection with any release from the security and other interest created by Section 2.1 of any Lease Indenture of a portion of the Lease Indenture Estate (as defined in such Lease Indenture) pursuant to Section 2.3 of such Lease Indenture, APS will cause to be delivered to the Trustee a certificate of an engineer, appraiser or other expert as the fair value of any portion of the Lease Indenture Estate to be released from the lien of such Lease Indenture and such certificate shall state that in the opinion of the

person making the same the proposed release will not impair the security under such Lease Indenture in contravention of the provisions thereof. If the fair value of the portion of the Lease Indenture Estate to be released and all other portions of the Lease Indenture Estate released since the commencement of the then current calendar year, as set forth in the certificate required pursuant to this Section 5.12, is ten per centum (10%) or more of the aggregate principal amount of Securities at the time Outstanding, such certificate shall be made by an independent engineer, appraiser or other expert; *provided, that*, a certificate of an independent engineer, appraiser, or other expert is not required in the case of any release of portions of the Lease Indenture Estate if the fair market value thereof as set forth in the certificate or opinion required by this Section 5.12 is less than \$25,000 or less than 1 per centum (1%) of the aggregate principal amount of Securities at the time Outstanding.

ARTICLE SIX

REDEMPTION OF SECURITIES

The provisions of this Article Six shall be applicable to the Securities of any series which are redeemable before their Stated Maturity of principal except as otherwise provided in such Securities or the Series Supplemental Indenture with respect thereto as contemplated by Section 2.03.

SECTION 6.01. *Notice to Trustee of Redemption.*

In case of any redemption of any Securities of any series otherwise than through the operation of an applicable Sinking Fund, the Company shall, at least 45 days prior to the scheduled Redemption Date (unless a shorter notice shall be satisfactory to the Trustee), notify the Trustee in writing of such Redemption Date and of the principal amount of Securities of such series to be redeemed.

SECTION 6.02. *Selection by Trustee of Securities to be Redeemed.*

If fewer than all the Securities of any series are to be redeemed, other than through the operation of an applicable Sinking Fund, the particular Securities of such series to be redeemed shall be selected following receipt by the Trustee of the notice required by Section 6.01, but not more than 60 days prior to the Redemption Date, by the Trustee, from the Outstanding Securities of such series not previously called for redemption, as follows. To the extent any Pledged Lessor Note is being prepaid in connection with such redemption, the Trustee shall first identify the Securities of such series having Stated Maturities of principal which correspond to the maturities (including serial maturities within a single Pledged Lessor

Note) of the Pledged Lessor Note being prepaid, and shall then identify the amounts which have been prepaid in respect of such maturity (or serial maturity) of Pledged Lessor Note. Following such identification, the Trustee shall select for redemption an aggregate principal amount of Securities of such series of each Stated Maturity of principal equal to the aggregate principal amount of the maturity (or serial maturity) of the Pledged Lessor Note being prepaid, such selection to be made by lot as among all Securities having such Stated Maturity of principal, according to such method as the Trustee shall deem proper in its discretion; *provided, however*, that when Securities are being redeemed pursuant to any applicable optional (rather than mandatory) redemption provisions, the Securities to be redeemed shall be selected solely from the Securities of the series and of the Stated Maturity of principal in respect of which a Company Order has been received. In any such designation by lot the designation may be made from the numbers of the Securities of such series then Outstanding (1) in groups of consecutive numbers (including or excluding, for the purpose of such grouping, the numbers of Securities previously called for redemption or otherwise retired), or (2) individually from the numbers of all such Securities not previously called for redemption or otherwise retired, or (3) if there is any portion to be called which is but a fraction of a group, individually by lot from the several individual numbers in any such group so designated by lot.

The Trustee shall promptly notify the Company, APS, the Security Registrar and each Paying Agent in writing of the Securities selected for redemption and, in the case of any Security selected for partial redemption, 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 Security redeemed or to be redeemed only in part, to the portion of the principal of such Security which has been or is to be redeemed.

SECTION 6.03. *Notice of Redemption.*

Notice of redemption (including redemption through the operation of any applicable Sinking Fund) shall be given by first-class mail, postage prepaid, mailed not less than 20 nor more than 60 days prior to the Redemption Date, to each Holder of Securities to be redeemed, at his address appearing in the Security Register.

All notices of redemption shall state:

- (1) the Redemption Date,
- (2) the Redemption Price,
- (3) if fewer than all Outstanding Securities of any series are to be redeemed, the identification (and, in the case of partial redemption, the respective principal amounts) of the particular Securities, including the series and the Stated Maturity of principal of such Securities, to be redeemed,
- (4) that on the Redemption Date the Redemption Price will become due and payable upon each such Security, and that interest thereon shall cease to accrue from and after said date,
- (5) the place where such Securities are to be surrendered for payment of the Redemption Price, and
- (6) that the redemption is through the operation of a Sinking Fund, if such is the case.

Notice of redemption of Securities to be redeemed shall be given by the Trustee in the name of the Company.

SECTION 6.04. *Deposit of Redemption Price.*

Prior to any Redemption Date, the Company shall deposit, or cause to be deposited, with the Paying Agent an amount of money sufficient to pay the Redemption Price of all the Securities which are to be redeemed on that date.

SECTION 6.05. *Securities Payable on Redemption Date.*

Notice of redemption having been given as aforesaid, the Securities so to be redeemed shall, on the Redemption Date, become due and payable at the corporate trust office of the Paying Agent (or, if such office is not in the Borough of Manhattan, the City of New York, at either such office or an office to be maintained in such Borough) at the Redemption Price therein specified and from and after such date (unless there shall be a default in the payment of the Redemption Price) such Securities shall cease to bear interest. Upon surrender of such Securities for redemption in accordance with said notice, such Securities shall be paid at the Redemption Price, *exclusive, however,* of installments of interest maturing on or prior to the Redemption Date, payment of which shall have been made or duly provided

for to the Holders of such Securities registered as such on the relevant Record Dates, or otherwise, according to their terms and the provisions of Section 2.10.

If any Security called for redemption shall not be so paid upon surrender thereof for redemption, the principal (and premium, if any) shall, until paid, continue to bear interest from the Redemption Date at the rate borne by the Security in respect of overdue payments.

SECTION 6.06. *Securities Redeemed in Part.*

Any Security which is to be redeemed only in part shall be surrendered at the corporate trust office of the Paying Agent (or, if such office is not in the Borough of Manhattan, the City of New York, at either such office or an office to be maintained in such Borough) (with due endorsement by, or a written instrument of transfer in form satisfactory to the Security Registrar duly executed by, the Holder thereof or his attorney duly authorized in writing) and the Company shall execute and the Trustee shall authenticate and deliver to the Paying Agent for delivery to the Holder of such Security a new Security or Securities of the same series and the same Stated Maturity of principal, of any authorized denomination as requested by such Holder in aggregate principal amount equal to and in exchange for the unredeemed portion of the principal of the Security so surrendered.

ARTICLE SEVEN

SINKING FUNDS

SECTION 7.01. *Sinking Funds for Securities.*

The amount of any sinking fund payment provided for by the terms of Securities of any series (and any Stated Maturity of principal within a series) is herein referred to as a "*Sinking Fund*", and the date on which a Sinking Fund payment is to be made is herein referred to as a "*Sinking Fund Date*." Each such Sinking Fund payment shall be applied to the redemption of Securities of the appropriate series and the appropriate Stated Maturity of principal on the appropriate Sinking Fund Date.

In the event that there shall have been any partial redemption of a series of Securities (other than pursuant to an applicable Sinking Fund), the Sinking Fund payments with respect to such series shall be adjusted as follows. The Trustee shall first identify the maturity (or serial maturity

within a Pledged Lessor Note) of the Pledged Lessor Note or Notes, if any, in respect of which a prepayment shall have been made and, having so identified such maturity, shall determine the dates on which the principal of such Pledged Lessor Notes were scheduled to be amortized (the "Scheduled Amortization Dates"). The aggregate amount of Sinking Fund payments scheduled to be made on a Sinking Fund Date shall then be adjusted to equal the aggregate principal amount of all Pledged Lessor Notes scheduled to be amortized on the Scheduled Amortization Date corresponding to such Sinking Fund Date, after taking into account the prepayment of Pledged Lessor Notes, and the amount of each Sinking Fund payment shall be proportionately adjusted. All such adjustments in respect of a Sinking Fund Date shall be rounded to the nearest \$1,000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of Securities redeemed pursuant to such partial redemption. In connection with such adjustments, the Company shall deliver to the Trustee a Company Request not later than 60 days prior to the next Sinking Fund Date following any partial redemption of a series of Securities (other than pursuant to an applicable Sinking Fund) setting forth a revised schedule of Sinking Fund payments applicable to such series of Securities. The Trustee may rely on such Company Request and shall have no duty with respect to the adjustments set forth therein other than to make them available for inspection by a Holder of such series of Securities at the Corporate Trust Office upon reasonable notice.

SECTION 7.02. *Selection by Trustee of Securities to Be Redeemed Through Operation of Sinking Fund.*

In the case of Securities to be redeemed through operation of an applicable Sinking Fund, the particular Securities to be redeemed shall be selected no more than 60 days nor less than 30 days prior to the Redemption Date by the Trustee from the Outstanding Securities of the same series and of the same Stated Maturity of principal not previously called for redemption by lot as among all Securities having such Stated Maturity. In any such designation by lot the designation may be made from the numbers of the Securities of such series then Outstanding (1) in groups of consecutive numbers (including or excluding, for the purpose of such grouping, the numbers of Securities previously called for redemption or otherwise retired), or (2) individually from the numbers of all such Securities not previously called for redemption or otherwise retired, or (3) if there is any

portion to be called which is but a fraction of a group, individually by lot from the several individual numbers in any such group so designated by lot.

ARTICLE EIGHT

EVENTS OF DEFAULT; REMEDIES

SECTION 8.01. *Events of Default.*

"Events of Default", wherever used herein, 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 a judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

(1) default in the payment of any interest upon any Security when it becomes due and payable, and continuance of such default for a period of ten (10) days; or

(2) default in the payment of the principal of (or premium, if any, on) any Security at its Stated Maturity, or upon call for redemption or otherwise, and continuance of such default for a period of ten (10) days; or

(3) default in the making of any Sinking Fund payment, and continuance of such default for a period of ten (10) days; or

(4) default in the performance, or breach, of any covenant of APS or the Company contained herein and continuance of such default or breach for a period of 30 days after there has been given, by registered or certified mail, to APS and the Company by the Trustee, or to APS, the Company and the Trustee by the Holders of at least 25% in principal amount of Outstanding Securities, a written notice specifying such failure and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder; or

(5) the occurrence of an "event of default" under any Lease Indenture; or

(6) the entry of a decree or order by a court having jurisdiction in the premises adjudging the Company a bankrupt or insolvent, or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition of or in respect of the Company under the Federal Bankruptcy Act or any other applicable federal or state

law or law of the District of Columbia, or appointing a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company or of any substantial part of its property, or ordering the winding up or liquidation of its affairs, and the continuance of any such decree or order unstayed and in effect for a period of 75 consecutive days; or

(7) the institution by the Company 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 the Federal Bankruptcy Code or any other applicable federal or state law or law of the District of Columbia, or the consent by it to the filing of any such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company 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 corporate action by the Company in furtherance of any such action.

SECTION 8.02. *Acceleration of Maturity; Rescission and Annulment.*

Upon the occurrence of an Event of Default, (i) if such Event of Default is one referred to in clause (1), (2), (3), (4), (6) or (7) of Section 8.01, the Trustee may, and upon the direction of the Holders of not less than a majority in principal amount of the Securities Outstanding shall, and (ii) if such Event of Default is the one referred to in clause (5) of Section 8.01 (including without limitation an event of default under any Lease which has resulted in an Event of Default referred to in clause (1), (2), or (3) of Section 8.01) under circumstances in which the Pledged Lessor Notes have been declared immediately due and payable, the Trustee shall, declare the principal of all the Securities to be due and payable immediately, by a notice in writing to APS and the Company, and upon any such declaration such principal shall become immediately due and payable; provided that no such declaration shall be made (and no action under Section 8.03 or 8.05 shall be taken) in cases in which the Event of Default is one referred to in clause (1), (2), or (3) of Section 8.01 which resulted directly from a failure of APS to make any payment of rent under any Lease until such time as the Lessor under such Lease has been given the opportunity to exercise its rights, if any, under provisions of the related

Lease Indenture analogous to Section 6.8 of the Lease Indentures dated as of August 1, 1986.

At any time after such a declaration of acceleration has been made and before any sale of the Pledged Property, or any part thereof, shall have been made pursuant to any power of sale as hereinafter in this Article *provided*, the Holders of a majority in principal amount of the Securities Outstanding, by written notice to the Company and the Trustee, may rescind and annul such declaration and its consequences if

(1) there shall have been paid to or deposited with the Trustee a sum sufficient to pay

(A) all overdue installments of interest on all Securities,

(B) the principal of (and premium, if any, on) any Securities which have become due otherwise than by such declaration of acceleration and interest thereon at the respective rates provided in the Securities for late payments of principal or premium,

(C) to the extent that payment of such interest is lawful, interest upon overdue installments of interest at the respective rates provided in the Securities for late payments of interest, and

(D) all sums paid or advanced by the Trustee hereunder and the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel, and

(2) all Events of Default, other than the non-payment of the principal of Securities which have become due solely by such acceleration, have been cured or waived as provided in Section 8.08.

No such rescission shall affect any subsequent default or impair any right consequent thereon and no such annulment shall take place unless all declarations of acceleration of all Pledged Lessor Notes theretofore given have also been annulled in accordance with the terms of the applicable Lease Indentures.

Notwithstanding anything in this Section to the contrary, the Trustee shall rescind any declaration of maturity of the principal of and interest on the Securities as a consequence of an Event of Default which resulted from an event of default under any Lease and which resulted in a declaration of acceleration of the Pledged Lessor Notes issued under the related Lease Indenture, if the declaration of acceleration of such Lessor Notes has been

rescinded in accordance with the terms of such Lease Indenture and the conditions set forth in paragraphs (1) and (2) of this Section have been met.

SECTION 8.03. *Trustee's Power of Sale of Pledged Property; Notice Required; Power to Bring Suit.*

If an Event of Default shall have occurred and be continuing, subject to the provisions of Sections 8.06 and 8.07 and the proviso to the first paragraph of Section 8.02, the Trustee, by such officer or agent as it may appoint, may:

(1) sell, to the extent permitted by law, without recourse, for cash, or credit or for other property, for immediate or future delivery, and for such price or prices and on such terms as the Trustee in its discretion may determine, the Pledged Property as an entirety, or in any such portions as the Holders of a majority in aggregate principal amount of the Securities then Outstanding shall request by an Act of Securityholders, or, in the absence of such request, as the Trustee in its discretion shall deem expedient in the interest of the Securityholders, at public or private sale; and/or

(2) proceed by one or more suits, actions or proceedings at law or in equity or otherwise or by any other appropriate remedy, to enforce payment of the Securities or Pledged Lessor Notes, or to foreclose this Indenture or to sell the Pledged Property under a judgment or decree of a court or courts of competent jurisdiction, or by the enforcement of any such other appropriate legal or equitable remedy, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce any of its rights or powers or any of the rights or powers of the Securityholders.

In the event that the Trustee shall deem it advisable to sell any of or all the Pledged Property in accordance with the provisions of this Section, APS and the Company agree that if registration of any such Pledged Property shall be required, in the opinion of counsel for the Trustee, under the Securities Act of 1933 or other applicable law, and regulations promulgated thereunder, and if APS shall not effect, or cause to be effected, such registration promptly, the Trustee may sell any such Pledged Property at a private sale, and no Person shall attempt to maintain that the prices at which such Pledged Property is sold are inadequate by reason of the failure to sell at public sale, or hold the Trustee liable therefor.

SECTION 8.04. *Incidents of Sale of Pledged Property.*

Upon any sale of all or any part of the Pledged Property made either under the power of sale given under this Indenture or under judgment or decree in any judicial proceedings for foreclosure or otherwise for the enforcement of this Indenture, the following shall be applicable:

(1) *Securities Due and Payable.* The principal of, and premium, if any, and accrued interest on, the Securities, if not previously due, shall immediately become and be due and payable.

(2) *Trustee Appointed Attorney of Company to Make Conveyances.* The Trustee is hereby irrevocably appointed the true and lawful attorney of the Company, in its name and stead, to make all necessary deeds, bills of sale and instruments of assignment, transfer or conveyance of the property thus sold; and for that purpose the Trustee may execute all such documents and instruments and may substitute one or more persons with like power; and the Company hereby ratifies and confirms all that its said attorneys, or such substitute or substitutes, shall lawfully do by virtue hereof.

(3) *Company to Confirm Sales and Conveyances.* If so requested by the Trustee or by any purchaser, the Company shall ratify and confirm any such sale or transfer by executing and delivering to the Trustee or to such purchaser or purchasers all proper deeds, bills of sale, instruments of assignment, conveyance or transfer and releases as may be designated in any such request.

(4) *Securityholders and Trustee May Purchase Pledged Property.* Any Securityholder or the Trustee may bid for and purchase any of the Pledged Property, and upon compliance with the terms of sale, may hold, retain, possess and dispose of such Pledged Property in his or its own absolute right without further accountability.

(5) *Purchaser at Sale May Apply Securities to Purchase Price.* Any purchaser at any such sale may, in paying the purchase price, deliver any of the Securities then Outstanding in lieu of cash and apply to the purchase price the amount which shall, upon distribution of the net proceeds of such sale, after application to the costs of the action and any other sums which the Trustee is authorized to deduct under this Indenture, be payable on such Securities so delivered in respect of principal, premium, if any, and interest. In case the amount so payable on such Securities shall be less than the amount due

thereon, duly executed and authenticated Securities shall be delivered in exchange therefor to the Holder thereof for the balance of the amount due on such Securities so delivered by such Holder.

(6) *Receipt of Trustee Shall Discharge Purchaser.* The receipt of the Trustee or of the officer making such sale under judicial proceedings shall be a sufficient discharge to any purchaser for his purchase money, and, after paying such purchase money and receiving such receipt, such purchaser or his personal representative or assigns shall not be obliged to see to the application of such purchase money, or be in any way answerable for any loss, misapplication or non-application thereof.

(7) *Sale To Divest Rights of Company in Property Sold.* Any such sale shall operate to divest the Company of all right, title, interest, claim and demand whatsoever, either at law or in equity or otherwise, in and to the Pledged Property so sold, and shall be a perpetual bar both at law and in equity or otherwise against the Company, and its successors and assigns, and any and all persons claiming or who may claim the Pledged Property sold or any part thereof from, through or under the Company, or its successors and assigns.

(8) *Application of Moneys Received upon Sale.* Any moneys collected by the Trustee upon any sale made either under the power of sale given by this Indenture or under judgment or decree in any judicial proceedings for foreclosure or otherwise for the enforcement of this Indenture, shall be applied as provided in Section 8.12.

SECTION 8.05. *Judicial Proceedings Instituted by Trustee.*

(a) *Trustee May Bring Suit.* If there shall be a failure to make payment of the principal of any Security at its Stated Maturity or upon declaration of acceleration, call for redemption or otherwise, or of any Sinking Fund payment when due and payable by the terms hereof or of such Security, or if there shall be a failure to pay the premium, if any, or interest on any Security when the same becomes due and payable, then the Trustee, if any such failure shall continue for 15 days, in its own name, and as trustee of an express trust, shall be entitled, and empowered subject to the proviso to the first paragraph of Section 8.02 to institute any suits, actions or proceedings at law, in equity or otherwise, for the collection of the sums so due and unpaid on the Securities, and may prosecute any such claim or

proceeding to judgment or final decree, and may enforce any such judgment or final decree and collect the moneys adjudged or decreed to be payable in any manner provided by law, whether before or after or during the pendency of any proceedings for the enforcement of the Lien of this Indenture, or of any of the Trustee's rights or the rights of the Securityholders under this Indenture, and such power of the Trustee shall not be affected by any sale hereunder or by the exercise of any other right, power or remedy for the enforcement of the provisions of this Indenture, or for the foreclosure of the lien hereof.

(b) *Trustee May Recover Unpaid Indebtedness after Sale of Pledged Property.* In the case of a sale of the Pledged Property and of the application of the proceeds of such sale to the payment of the indebtedness secured by this Indenture, the Trustee in its own name, and as trustee of an express trust, shall be entitled and empowered, by any appropriate means, legal, equitable or otherwise, to enforce payment of, and to receive all amounts then remaining due and unpaid upon, all or any of the Securities, for the benefit of the Holders thereof, and upon any other portion of the indebtedness remaining unpaid, with interest at the rates specified in the respective Securities on the overdue principal of and premium, if any, and (to the extent that payment of such interest is legally enforceable) on the overdue installments of interest.

(c) *Recovery of Judgment Does Not Affect Lien of this Indenture or Other Rights.* No recovery of any such judgment or final decree by the Trustee and no levy of any execution under any such judgment upon any of the Pledged Property, or upon any other property, shall in any manner or to any extent affect the Lien of this Indenture upon any of the Pledged Property, or any rights, powers or remedies of the Trustee, or any liens, rights, powers or remedies of the Securityholders, but all such liens, rights, powers and remedies shall continue unimpaired as before.

(d) *Trustee May File Proofs of Claim; Appointment of Trustee as Attorney-in-Fact in Judicial Proceedings.* The Trustee in its own name, or as trustee of an express trust, or as attorney-in-fact for the Securityholders, or in any one or more of such capacities (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 for the payment of overdue principal, premium (if any) or interest), shall be entitled and empowered to file such proofs of claim and other papers or documents as may be necessary or

advisable in order to have the claims of the Trustee and of the Securityholders (whether such claims be based upon the provisions of the Securities or of this Indenture) allowed in any equity, receivership, insolvency, bankruptcy, liquidation, readjustment, reorganization or any other judicial proceedings relative to the Company or any obligor on the Securities (within the meaning of the TIA), the creditors of the Company or any such obligor, the Pledged Property or any other property of the Company or any such obligor and any receiver, assignee, trustee, liquidator, sequesteror (or other similar official) in any such judicial proceeding is hereby authorized by each Securityholder 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 Securityholders, to pay to the Trustee any amount due to it for the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel. The Trustee is hereby irrevocably appointed (and the successive respective Holders of the Securities, by taking and holding the same, shall be conclusively deemed to have so appointed the Trustee) the true and lawful attorney-in-fact of the respective Securityholders, with authority to (i) make and file in the respective names of the Securityholders (subject to deduction from any such claims of the amounts of any claims filed by any of the Securityholders themselves), any claim, proof of claim or amendment thereof, debt, proof of debt or amendment thereof, petition or other document in any such proceedings and to receive payment of any amounts distributable on account thereof, (ii) execute any such other papers and documents and to do and perform any and all such acts and things for and on behalf of such Securityholders, as may be necessary or advisable in order to have the respective claims of the Trustee and of the Securityholders against the Company or any such obligor, the Pledged Property or any other property of the Company or any such obligor allowed in any such proceeding and (iii) receive payment of or on account of such claims and debt; *provided, however*, that nothing contained in this Indenture shall be deemed to give to the Trustee any right to accept or consent to any plan of reorganization or otherwise by action of any character in any such proceeding to waive or change in any way any right of any Securityholder. Any moneys collected by the Trustee under this Section shall be applied as provided in Section 8.12.

(e) *Trustee Need Not Have Possession of Securities.* All rights of action and of asserting claims under this Indenture or under any of the Securities enforceable by the Trustee may be enforced by the Trustee

without possession of any of such Securities or the production thereof at the trial or other proceedings relative thereto.

(f) *Suit To Be Brought for Ratable Benefit of Securityholders.* Any suit, action or other proceeding at law, in equity or otherwise which shall be instituted by the Trustee under any of the provisions of this Indenture shall be for the equal, ratable and common benefit of all the Securityholders, subject to the provisions of this Indenture.

(g) *Trustee May Be Restored to Former Position and Rights in Certain Circumstances.* In case the Trustee shall have proceeded to enforce any right under this Indenture by suit, foreclosure or otherwise and such proceedings shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee, then in every such case, APS, the Company and the Trustee shall be restored without further act to their respective former positions and rights hereunder, and all rights, remedies and powers of the Trustee shall continue as though no such proceedings had been taken.

SECTION 8.06. *Securityholders May Demand Enforcement of Rights by Trustee.*

If an Event of Default shall have occurred and shall be continuing, the Trustee shall, upon the written request of the Holders of a majority in aggregate principal amount of the Securities then Outstanding and upon the offering of indemnity as provided in Section 9.03(e), but subject in all cases to the provisions of Section 3.03 and the proviso to the first paragraph of Section 8.02, proceed to institute one or more suits, actions or proceedings at law, in equity or otherwise, or take any other appropriate remedy, to enforce payment of the principal of, or premium, if any, or interest on, the Securities or Pledged Lessor Notes or to foreclose this Indenture or to sell the Pledged Property under a judgment or decree of a court or courts of competent jurisdiction or under the power of sale herein granted, or take such other appropriate legal, equitable or other remedy, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce any of the rights or powers of the Trustee or the Securityholders, or, in case such Securityholders shall have requested a specific method of enforcement permitted hereunder, in the manner requested, provided that such action shall not be otherwise than in accordance with law and the provisions of this Indenture, and the Trustee, subject to such indemnity provisions, shall have the right to decline to follow any such request if the Trustee in good faith

shall determine that the suit, proceeding or exercise of the remedy so requested would involve the Trustee in personal liability or expense.

SECTION 8.07. *Control by Securityholders.*

The Holders of a majority in principal amount of the Outstanding Securities 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, provided that

(1) such direction shall not be in conflict with any rule of law or with this Indenture, and

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

SECTION 8.08. *Waiver of Past Defaults.*

The Holders of not less than a majority in principal amount of the Outstanding Securities may on behalf of the Holders of all the Securities waive any past default hereunder and its consequences, except that only the Holders of all Securities affected thereby may waive a default

(1) in the payment of the principal of (or premium, if any) or interest on such Securities, or

(2) in respect of a covenant or provision hereof which under Article Eleven cannot be modified or amended without the consent of the Holder of each Outstanding Security affected.

Upon any such waiver, such default shall cease to exist, and any Event 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 8.09. *Securityholder May Not Bring Suit Except under Certain Conditions.*

A Securityholder shall not have the right to institute any suit, action or proceeding at law or in equity or otherwise for the foreclosure of this Indenture, for the appointment of a receiver or for the enforcement of any other remedy under or upon this Indenture, unless:

(1) such Securityholder previously shall have given written notice to the Trustee of a continuing Event of Default;

(2) the Holders of at least 25% in aggregate principal amount of the Securities then Outstanding shall have requested the Trustee in writing to institute such action, suit or proceeding and shall have offered to the Trustee indemnity as provided in Section 9.03(e);

(3) the Trustee shall have refused or neglected to institute any such action, suit or proceeding for 60 days after receipt of such notice, request and offer of indemnity; and

(4) no direction inconsistent with such written request has been given to the Trustee during such 60-day period by the Holders of a majority in principal amount of Outstanding Securities.

It is understood and intended that no one or more of the Securityholders shall have any right in any manner whatever hereunder or under the Securities to (i) surrender, impair, waive, affect, disturb or prejudice the Lien of this Indenture on any property subject thereto or the rights of the Holders of any other Securities, (ii) obtain or seek to obtain priority or preference over any other such Holder or (iii) enforce any right under this Indenture, except in the manner herein provided and for the equal, ratable and common benefit of all the Securityholders subject to the provisions of this Indenture.

SECTION 8.10. *Undertaking To Pay Court Costs.*

All parties to this Indenture, and each Securityholder by his acceptance of a Security, shall be deemed to have agreed that any court may in its discretion require, in any suit, action or proceeding for the enforcement of any right or remedy under this Indenture, or in any suit, action or proceeding against the Trustee for any action taken or omitted by it as Trustee hereunder, the filing by any party litigant in such suit, action or proceeding of an undertaking to pay the costs of such suit, action or proceeding, and that such court may, in its discretion, assess reasonable costs, including reasonable attorneys' fees, against any party litigant in such suit, action or proceeding, having due regard to the merits and good faith of the claims or defenses made by such party litigant; provided, however, that the provisions of this Section shall not apply to (a) any suit, action or proceeding instituted by the Trustee, (b) any suit, action or proceeding instituted by any Securityholder or group of Securityholders

holding in the aggregate more than 10% in aggregate principal amount of the Securities then Outstanding or (c) any suit, action or proceeding instituted by any Securityholder for the enforcement of the payment of the principal of, or premium, if any, or interest on, any of the Securities, on or after the respective due dates expressed therein.

SECTION 8.11. *Right of Securityholders To Receive Payment Not To Be Impaired.*

Anything in this Indenture to the contrary notwithstanding, the right of any Holder of any Security to receive payment of the principal of, and premium, if any, and interest on, such Security, on or after the respective due dates expressed in such Security (or, in case of redemption, on the Redemption Date fixed for such Security), or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected without the consent of such Holder.

SECTION 8.12. *Application of Moneys Collected by Trustee.*

Any moneys collected or to be applied by the Trustee pursuant to this Article, together with any other moneys which may then be held by the Trustee under any of the provisions of this Indenture as security for the Securities (other than moneys at the time required to be held for the payment of specific Securities at their Stated Maturities or at a time fixed for the redemption thereof) shall be applied in the following order from time to time, on the date or dates fixed by the Trustee and, in the case of a distribution of such moneys on account of principal, premium, if any, or interest, upon presentation of the several Outstanding Securities, and stamping thereon of payment, if only partially paid, and upon surrender thereof, if fully paid:

FIRST: to the payment of all taxes, assessments or liens prior to the Lien of this Indenture, except those subject to which any sale shall have been made, all reasonable costs and expenses of collection, including the reasonable costs and expenses of handling the Pledged Property and of any sale thereof pursuant to the provisions of this Article and of the enforcement of any remedies hereunder or under any Lease Indenture, and to the payment of all amounts due the Trustee or any predecessor Trustee under Section 9.07, or through the Trustee by any Securityholder or Securityholders;

SECOND: in case the principal of the Securities or any of them shall not have become due, to the payment of any interest in default, in the order of the maturity of the installments of such interest, with interest at the rates specified in the respective Securities in respect of overdue payments (to the extent that payment of such interest shall be legally enforceable) on the overdue installments thereof;

THIRD: in case the principal of any of but not all the Securities shall have become due at their Stated Maturities, upon redemption or otherwise, first to the payment of accrued interest in the order of the maturity of the installments thereof with interest at the respective rates specified in the Securities in respect of payments on overdue principal, premium, if any, and (to the extent that payment of such interest shall be legally enforceable) on overdue installments of interest, and next to the payment of the principal of all Securities then due;

FOURTH: in case the principal of all the Securities shall have become due at their Stated Maturities, by declaration, upon redemption or otherwise, to the payment of the whole amount then due and unpaid upon the Securities then Outstanding for principal, premium, if any, and interest, together with interest at the respective rates specified in the Securities in respect of overdue payments on principal, premium, if any, and (to the extent that payment of such interest shall be legally enforceable) on overdue installments of interest, and, in case such proceeds shall be insufficient to pay in full the whole amount so due and unpaid, then to the payment of such principal, premium, if any, and interest ratably, without discrimination or preference; and

FIFTH: in case the principal of all the Securities shall have become due at their Stated Maturities, by declaration, upon redemption or otherwise, and all of such Securities shall have been fully paid, together with all interest (including any interest on overdue payments) and premium, if any, thereon, any surplus then remaining shall be paid to the Company, its successors or assigns, or to whomsoever may be lawfully entitled to receive the same, or as a court of competent jurisdiction may direct;

provided, however, that all payments to be made pursuant to this Section shall be made ratably to the persons entitled thereto, without discrimination or preference.

SECTION 8.13. *Securities Held by Certain Persons Not To Share in Distribution.*

Any Securities known to the Trustee to be owned or held by, or for the account or benefit of, APS, the Company or any Affiliate of any thereof shall not be entitled to share in any payment or distribution provided for in this Article until all Securities held by other Persons have been paid in full.

SECTION 8.14. *Waiver of Appraisalment, Valuation, Stay, Right to Marshalling.*

To the extent it may lawfully do so, each of APS and the Company, for itself and for any Person who may claim through or under it, hereby:

(1) agrees that neither it nor any such Person will set up, plead, claim or in any manner whatsoever take advantage of, any appraisalment, valuation, stay, extension or redemption laws, now or hereafter in force in any jurisdiction, which may delay, prevent or otherwise hinder (i) the performance or enforcement or foreclosure of this Indenture, (ii) the sale of any of the Pledged Property, or (iii) the putting of the purchaser or purchasers thereof into possession of such property immediately after the sale thereof;

(2) waives all benefit or advantage of any such laws;

(3) waives and releases all rights to have the Pledged Property marshalled upon any foreclosure, sale or other enforcement of this Indenture; and

(4) consents and agrees that all the Pledged Property may at any such sale be sold by the Trustee as an entirety.

SECTION 8.15. *Remedies Cumulative; Delay or Omission Not a Waiver.*

Every remedy given hereunder to the Trustee or to any of the Securityholders shall not be exclusive of any other remedy or remedies, and every such remedy shall be cumulative and in addition to every other remedy given hereunder or now or hereafter given by statute, law, equity or otherwise. The Trustee may exercise all or any of the powers, rights or remedies given to it hereunder or which may now or hereafter be given by statute, law or equity or otherwise, in its absolute discretion. No course of dealing between APS or the Company and the Trustee or the Securityholders or any delay or omission of the Trustee or of any Securityholder to exercise any right, remedy or power accruing upon any Event of Default

shall impair any such right, remedy or power or shall be construed to be a waiver of any such Event of Default or of any right of the Trustee or of the Securityholders or acquiescence therein, and, subject to the provisions of Section 8.07, every right, remedy and power given by this Article to the Trustee or to the Securityholders may be exercised from time to time and as often as may be deemed expedient by the Trustee or by the Securityholders.

ARTICLE NINE

THE TRUSTEE

SECTION 9.01. *Certain Duties and Responsibilities.*

(a) Except during the continuance of an Event of Default,

(1) the Trustee undertakes to perform 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

(2) in the absence of bad faith on its part, the Trustee may 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 has occurred and is continuing, the Trustee shall exercise 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

(1) this Subsection shall not be construed to limit the effect of Subsection (a) of this Section;

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

(3) 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 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; and

(4) 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 herein 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 9.02. *Notice of Defaults.*

In addition to its obligation to give notice to Securityholders as provided in Section 3.03, as promptly as practicable after, and in any event within 90 days after, the occurrence of any default hereunder, the Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, notice of such default hereunder actually known by an officer in the corporate trustee administration department of the Trustee, unless such default shall have been cured or waived; *provided, however,* that, except in the case of a default in the payment of the principal of (or premium, if any) or interest on any Security or in the payment of any Sinking Fund installment, the 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 Trustee in good faith determine that the withholding of such notice is in the interests of the Securityholders; and *provided, further,* that in the case of any default of the character specified in Section 8.01(4) no such notice to Securityholders shall be given until at least 30 days after the occurrence

thereof. 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 9.03. *Certain Rights of Trustee.*

Except as otherwise provided in Section 9.01:

(a) the Trustee may rely and shall be protected in acting or refraining from acting in reliance upon any resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order, bond, debenture 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) any request or direction of APS or the Company mentioned herein shall be sufficiently evidenced by an APS or Company Request or Order, in the case of a request or direction of APS, the Company, as the case may be and any resolution of the Board of Directors of APS or the Company may be sufficiently evidenced by a Board Resolution of APS or the Company, as the case may be;

(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 be herein specifically prescribed) may, in the absence of bad faith on its part, rely upon an Officers' Certificate of APS or the Company;

(d) the Trustee may consult with counsel and the 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 of the Securityholders pursuant to this Indenture, unless such Securityholders shall have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities which might be incurred by it in compliance 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 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 be entitled to examine the books, records and premises of APS or the Company, personally or by agent or attorney; and

(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.

SECTION 9.04. *Not Responsible for Recitals or Issuance of Securities.*

The recitals contained herein and in the Securities, except the certificates of authentication, shall not be taken as the statements of the Trustee, and the Trustee assumes no responsibility for their correctness. The Trustee makes no representations as to the validity or sufficiency of this Indenture, the Pledged Property or the Securities, except that the Trustee hereby represents and warrants that this Indenture has been executed and delivered by one of its officers who is duly authorized to execute and deliver such document on its behalf. The Trustee shall not be accountable for the use or application by the Company of Securities or the proceeds thereof.

SECTION 9.05. *May Hold Securities.*

The Trustee, any Paying Agent, Security Registrar or any other agent of APS or the Company, in its individual or any other capacity, may become the owner or pledgee of Securities and, subject to Sections 9.08 and 9.13, may otherwise deal with APS and the Company with the same rights it would have if it were not Trustee, Paying Agent, Security Registrar or such other agent.

SECTION 9.06. *Funds May Be Held by Trustee or Paying Agent; Investments.*

(a) Subject to subsection (b) of this Section 9.06, any monies held by the Trustee or the Paying Agent hereunder as part of the Pledged Property

may, until paid out by the Trustee or the Paying Agent as herein provided, be carried by the Trustee or the Paying Agent on deposit with itself, and neither the Trustee nor the Paying Agent shall have any liability for interest upon any such monies.

(b) At any time and from time to time prior to payment in full of any amounts to be paid by the Trustee pursuant to Section 2.15(b) in respect of any series of Securities (or prior to payment in full of any amount required to be paid by the Trustee in respect of such series of Securities pursuant to the applicable provisions of the Series Supplemental Indenture relating thereto if such series of Securities is to be authenticated in advance of the actual delivery to the Trustee of the Pledged Lessor Notes relating thereto) if at the time no Event of Default has occurred and is continuing, the Trustee shall, on Company Request, invest and reinvest in Permitted Investments as specified in such Company Request any monies from the sale of the Securities of such series at the time on deposit with the Trustee as part of the Pledged Property, together with any income and gains from the investment and reinvestment thereof, and sell any Permitted Investments, in either case, at such prices, including accrued interest, as are set forth in such Company Request, and such Permitted Investments shall be held by the Trustee until so sold in trust as part of the Pledged Property. The Trustee shall, on Company Request, sell such Permitted Investments as may be specified therein, and the Trustee shall, without Company Request, in the event monies are required for payment of any amounts to be paid by the Trustee pursuant to Section 2.15(b) in respect of any series of Securities and for any Stated Maturity of any installment of interest on any series of Securities becoming due and payable prior to the thirtieth day following the Termination Date applicable to such series, sell such Permitted Investments as are required to restore to cash as part of the Pledged Property such amounts as are needed for any such payment. The Trustee shall not be responsible for any losses on any investments or sales of Permitted Investments made pursuant to the procedure specified in this subsection (b).

Section 9.07. Compensation and Reimbursement.

The Company agrees

(1) to pay, or cause to be paid, to each of the Trustee and any Authorized Agent 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);

(2) to reimburse, or cause to be reimbursed, each of the Trustee and any Authorized Agent upon its request for all expenses, disbursements and advances incurred or made by it in accordance with any provision of this Indenture (including the compensation and the expenses and disbursements of its agents and counsel), except any such expense, disbursement or advance as may be attributable to its own negligence, willful misconduct or bad faith; and

(3) to indemnify, or cause to be indemnified, each of the Trustee, any predecessor Trustee and any Authorized Agent for, and to hold it harmless against, any loss, liability or expense incurred without negligence, willful misconduct or bad faith on its part, arising out of or in connection with the acceptance or administration of this trust or the performance of its duties hereunder, including the 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.

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, except funds held in trust for the payment of principal of (and premium, if any) or interest on particular Securities.

SECTION 9.08. *Disqualification; Conflicting Interests.*

(a) If the Trustee has or shall acquire any conflicting interest, as defined in this Section, it shall, within 90 days after ascertaining that it has such conflicting interest, either eliminate such conflicting interest or resign in the manner and with the effect hereinafter specified in this Article.

(b) In the event that the Trustee shall fail to comply with the provisions of Subsection (a) of this Section the Trustee shall, within 10 days after the expiration of such 90-day period, transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, notice of such failure.

(c) For the purposes of this Section, the Trustee shall be deemed to have a conflicting interest if

(1) the Trustee is trustee under another Indenture under which any other securities, or certificates of interest or participation in any

other securities, of any obligor on the Securities are outstanding, unless (A) the Securities are collateral trust bonds under which the only collateral consists of securities issued under such other indenture, or (B) such other indenture is a collateral trust indenture under which the only collateral consists of Securities issued under this Indenture, provided that there shall be excluded from the operation of this paragraph any indenture or indentures under which other securities, or certificates of interest or participation in other securities, of such obligor are outstanding, if such obligor shall have sustained the burden of proving, on application to the Commission and after opportunity for hearing thereon, that trusteeship under this Indenture and such other indenture or indentures is not so likely to involve a material conflict of interest as to make it necessary in the public interest or for the protection of investors to disqualify the Trustee from acting as such under one of such indentures;

(2) the Trustee or any of its directors or executive officers is an obligor upon the Securities or an underwriter for such obligor;

(3) the Trustee directly or indirectly controls or is directly or indirectly controlled by or is under direct or indirect common control with any obligor on the Securities or an underwriter for such obligor;

(4) the Trustee or any of its directors or executive officers is a director, officer, partner, employee, appointee or representative of any obligor on the Securities, or of an underwriter (other than the Trustee itself) for such obligor who is currently engaged in the business of underwriting, except that (i) one individual may be a director or an executive officer, or both, of the Trustee and a director or an executive officer, or both, of an obligor on the Securities but may not be at the same time an executive officer of both the Trustee and such obligor; (ii) if and so long as the number of directors of the Trustee in office is more than nine, one additional individual may be director or an executive officer, or both, of the Trustee and a director of an obligor on the Securities; and (iii) the Trustee may be designated by an obligor on the Securities or by any underwriter for such obligor to act in the capacity of transfer agent, registrar, custodian, paying agent, fiscal agent, escrow agent, or depository, or in any other similar capacity, or, subject to the provisions of paragraph (1) of this Subsection, to act as trustee, whether under an indenture or otherwise;

(5) 10% or more of the voting securities of the Trustee is beneficially owned either by any director, partner, or executive officer thereof, or 20% or more of such voting securities is beneficially owned, collectively, by any two or more of such persons; or 10% or more of the voting securities of the Trustee is beneficially owned either by an underwriter for any obligor on the Securities or by any director, partner or executive officer thereof, or is beneficially owned collectively by any two or more such persons;

(6) the Trustee is the beneficial owner of, or holds as collateral security for an obligation which is in default (as hereinafter in this Subsection defined), (i) 5% or more of the voting securities, or 10% or more of any other class of security, of any obligor on the Securities not including the Securities issued under this Indenture and securities issued under any other indenture under which the Trustee is also trustee, or (ii) 10% or more of any class of security of an underwriter for any obligor on the Securities;

(7) the Trustee is the beneficial owner of, or holds as collateral security for an obligation which is in default (as hereinafter in this Subsection defined), 5% or more of the voting securities of any person who, to the knowledge of the Trustee, owns 10% or more of the voting securities of, or controls directly or indirectly or is under direct or indirect common control with, any obligor on the Securities;

(8) the Trustee is the beneficial owner of, or holds collateral security for an obligation which is in default (as hereinafter in this Subsection defined), 10% or more of any class of security of any person who, to the knowledge of the Trustee, owns 50% or more of the voting securities of any obligor on the Securities; or

(9) the Trustee owns, on May 15 in any calendar year, in the capacity of executor, administrator, testamentary or inter vivos trustee, guardian, committee or conservator, or in any other similar capacity, an aggregate of 25% or more of the voting securities, or of any class of security, of any person, the beneficial ownership of a specified percentage of which would have constituted a conflicting interest under paragraphs (6), (7) or (8) of this Subsection. As to any such securities of which the Trustee acquired ownership through becoming executor, administrator, or testamentary trustee of an estate which included them, the provisions of the preceding sentence shall not apply, for a period of two years from the date of such acquisition to the

extent that such securities included in such estate do not exceed 25% of such voting securities or 25% of any such class of security. Promptly after May 15 in each calendar year, the Trustee shall make a check of its holdings of such securities in any of the above mentioned capacities as of such May 15. If any obligor upon the Securities fails to make payment in full of the principal of, or the premium, if any, or interest on, any of the Securities when and as the same becomes due and payable, and such failure continues for 30 days thereafter, the Trustee shall make a prompt check of its holdings of such securities in any of the above mentioned capacities as of the date of the expiration of such 30 day period, and after such date, notwithstanding the foregoing provisions of this paragraph, all such securities so held by the Trustee, with sole or joint control over such securities vested in it, shall, but only so long as such failure shall continue, be considered as though beneficially owned by the Trustee for the purposes of paragraphs (6), (7) and (8) of this Subsection.

The specification of percentages in paragraphs (5) to (9) inclusive, of this Subsection, shall not be construed as indicating that the ownership of such percentages of the securities of a person is or is not necessary or sufficient to constitute direct or indirect control for the purposes of paragraph (3) or (7) of this Subsection.

For the purposes of paragraphs (6), (7), (8) and (9) of this Subsection only, (i) the terms "security" and "securities" shall include only such securities as are generally known as corporate securities, but shall not include any note or other evidence of indebtedness issued to evidence an obligation to repay moneys loaned to a person by one or more banks, trust companies or banking firms, or any certificate of interest or participation in any such note or evidence of indebtedness; (ii) an obligation shall be deemed to be "in default" when a default in payment of principal shall have continued for 30 days or more and shall not have been cured; and (iii) the Trustee shall not be deemed to be the owner or holder of (A) any security which it holds as collateral security, as trustee or otherwise, for an obligation which is not in default as defined in clause (ii) above, or (B) any security which it holds as collateral security under this Indenture, irrespective of any default hereunder, or (C) any security which it holds as agent for collection, or as custodian, escrow agent, or depositary, or in any similar representative capacity.

Except as provided in the next preceding paragraph, the word "security" or "securities" as used in this Indenture shall mean any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit sharing agreement, collateral trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to purchase, any of the foregoing.

(d) For the purposes of this Section:

(1) The term "underwriter" when used with reference to any obligor on the Securities means every person who, within three years prior to the time as of which the determination is made, has purchased from such obligor with a view to, or has offered or sold for such obligor in connection with, the distribution of any security of such obligor outstanding at such time, or has participated or has had a direct or indirect participation in any such undertaking, or has participated or has had a participation in the direct or indirect underwriting of any such undertaking, but such term shall not include a person whose interest was limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission.

(2) The term "director" means any director of a corporation, or any individual performing similar functions with respect to any organization whether incorporated or unincorporated.

(3) The term "person" means an individual, a corporation, a partnership, an association, a joint-stock company, a trust, an unincorporated organization, or a government or political subdivision thereof. As used in this paragraph, the term "trust" shall include only a trust where the interest or interests of the beneficiary or beneficiaries are evidenced by a security.

(4) The term "voting security" means any security presently entitling the owner or holder thereof to vote in the direction or management of the affairs of a person, or any security issued under or pursuant to any trust, agreement or arrangement whereby a trustee or

trustees or agent or agents for the owner or holder of such security are presently entitled to vote in the direction or management of the affairs of a person.

(5) The term "obligor" means any obligor upon the Securities within the meaning of TIA.

(6) The term "executive officer" means the president, every vice president, every trust officer, the cashier, the secretary, and the treasurer of a corporation, and any individual customarily performing similar functions with respect to any organization whether incorporated or unincorporated, but shall not include the chairman of the board of directors.

(e) The percentages of the voting securities and other securities specified in this Section shall be calculated in accordance with the following provisions:

(1) A specified percentage of the voting securities of the Trustee, any obligor or any other person referred to in this Section (each of whom is referred to as a "person" in this paragraph) means such amount of the outstanding voting securities of such person as entitles the holder or holders thereof to cast such specified percentage of the aggregate votes which the holders of all the outstanding voting securities of such person are entitled to cast in the direction or management of the affairs of such person.

(2) A specified percentage of a class of securities of a person means such percentage of the aggregate amount of securities of the class outstanding.

(3) The term "amount", when used in regard to securities, means the principal amount if relating to evidences of indebtedness, the number of shares if relating to capital shares and the number of units if relating to any other kind of security.

(4) The term "outstanding" means issued and not held by or for the account of the issuer. The following securities shall not be deemed outstanding within the meaning of this definition:

(i) securities of an issuer held in a sinking fund relating to securities of the issuer of the same class;

(ii) securities of an issuer held in a sinking fund relating to another class of securities of the issuer, if the obligation evidenced by such other class of securities is not in default as to principal or interest or otherwise;

(iii) securities pledged by the issuer thereof as security for an obligation of the issuer not in default as to principal or interest or otherwise; and

(iv) securities held in escrow if placed in escrow by the issuer thereof;

provided, however, that any voting securities of an issuer shall be deemed outstanding if any person other than the issuer is entitled to exercise the voting rights thereof.

(5) A security shall be deemed to be of the same class as another security if both securities confer upon the holder or holders substantially the same rights and privileges; *provided, however*, that in the case of secured evidences of indebtedness, all of which are issued under a single indenture, differences in the interest rates or maturity dates of various series thereof shall not be deemed sufficient to constitute such series different classes; and *provided, further*, that, in the case of unsecured evidences of indebtedness, differences in the interest rates or maturity dates thereof shall not be deemed sufficient to constitute them securities of different classes, whether or not they are issued under a single indenture.

SECTION 9.09. *Corporate Trustee Required; Eligibility.*

There shall at all times be a Trustee hereunder which shall be a corporation organized and doing business under the laws of the United States of America or of any State, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least \$50,000,000, and subject to supervision or examination by Federal or State authority. If such corporation publishes reports of condition at least annually, pursuant to law or to the requirements of the aforesaid 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, it shall resign immediately in the manner and with the effect hereinafter specified in this Article.

SECTION 9.10. *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 under Section 9.11.

(b) The Trustee may resign at any time by giving written notice thereof to APS and the Company. If an instrument of acceptance by a successor Trustee shall not have been delivered to APS, the Company and the Trustee within 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.

(c) The Trustee may be removed at any time by Act of the Holders of a majority in principal amount of the Outstanding Securities, delivered to the Trustee, APS and to the Company.

(d) If at any time:

(i) the Trustee shall fail to comply with Section 9.08(a) after written request therefor by any Lessor or by any Securityholder who has been a bona fide Holder of a Security for at least 6 months, or

(ii) the Trustee shall cease to be eligible under Section 9.09 and shall fail to resign after written request therefor by any Lessor or by any such Securityholder, 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, (i) APS, acting after consultation with the Company, may remove the Trustee by Board Resolution or (ii) subject to Section 8.10, any Securityholder who has been a bona fide Holder of a Security for at least 6 months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the removal of the Trustee and the appointment of a successor Trustee.

(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, APS, acting after consultation with the Company, shall promptly appoint by Board Resolution a successor Trustee. If, within 1 year after such resignation, removal or incapability, or the occurrence of such vacancy, a successor Trustee shall be appointed by Act of the Holders of a majority in principal amount of the Outstanding Securities delivered to APS, the Company and the retiring Trustee, the successor Trustee so appointed shall, forthwith upon its acceptance of such appointment, become the successor Trustee and supersede the successor Trustee appointed by APS. If no successor Trustee shall have been so appointed by APS, acting after consultation with the Company, or by the Securityholders, and accepted appointment in the manner hereinafter provided, any Securityholder who has been a bona fide Holder of a Security for at least 6 months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the appointment of a successor Trustee.

(f) The Company shall give notice of each resignation and each removal of the Trustee and each appointment of a successor Trustee by mailing written notice of such event by first-class mail, postage prepaid, to the Holders of Securities as their names and addresses appear in the Security Register. Each notice shall include the name of the successor Trustee and the address of its Corporate Trust Office.

SECTION 9.11. *Acceptance of Appointment by Successor.*

Every successor Trustee appointed hereunder shall execute, acknowledge and deliver to APS, 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, deed or conveyance, shall become vested with all the rights, powers, trusts and duties of the retiring Trustee; but, on request of any Lessor, the Company or the successor Trustee, such retiring Trustee shall, upon payment of its charges, 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, subject nevertheless to its lien, if any, provided for in Section 9.07. Upon request of any such successor Trustee, APS and the Company shall execute any and all instruments for more fully and certainly

vesting in and confirming to such successor Trustee all such rights, powers and trusts.

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 9.12. *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 of 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 9.13. *Preferential Collection of Claims against any Obligor.*

(a) Subject to Subsection (b) of this Section, if the Trustee shall be or shall become a creditor, directly or indirectly, secured or unsecured, of any obligor on the Securities (as defined in Subsection (c) of this Section) within 4 months prior to a default, as defined in Subsection (c) of this Section, or subsequent to such a default, then, unless and until such default shall be cured, the Trustee shall set apart and hold in a special account for the benefit of the Trustee individually, the Holders of the Securities and the holders of other indenture securities (as defined in Subsection (c) of this Section):

(i) an amount equal to any and all reductions in the amount due and owing upon any claim as such creditor in respect of principal or interest, effected after the beginning of such 4 month period and valid as against any obligor on the Securities and its other creditors, except any such reduction resulting from the receipt or disposition of any property described in paragraph (ii) of this Subsection, or from the exercise of any right of set-off which the Trustee could have exercised if

a petition in bankruptcy had been filed by or against any such obligor upon the date of such default; and (ii) all property received by the Trustee in respect of any claim as such creditor, either as security therefor, or in satisfaction or composition thereof, or otherwise, after the beginning of such 4 month period, or an amount equal to the proceeds of any such property, if disposed of, subject, however, to the rights, if any, of any obligor on the Securities and its other creditors in such property or such proceeds.

Nothing herein contained, however, shall affect the right of the Trustee

(A) to retain for its own account (i) payments made on account of any such claim by any Person (other than an obligor on the Securities) who is liable thereon, and (ii) the proceeds of the bona fide sale of any such claim by the Trustee to a third person, and (iii) distributions made in cash, securities or other property in respect of claims filed against such obligor in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law;

(B) to realize, for its own account, upon any property held by it as security for any such claim, if such property was so held prior to the beginning of such 4 month period;

(C) to realize, for its own account, but only to the extent of the claim hereinafter mentioned, upon any property held by it as security for any such claim, if such claim was created after the beginning of such 4 month period and such property was received as security therefor simultaneously with the creation thereof, and if the Trustee shall sustain the burden of proving that at the time such property was so received the Trustee had no reasonable cause to believe that a default as defined in Subsection (c) of this Section would occur within 4 months; or

(D) to receive payment on any claim referred to in paragraph (B) or (C), against the release of any property held as security for such claim as provided in paragraph (B) or (C), as the case may be, to the extent of the fair value of such property.

For the purposes of paragraphs (B), (C) and (D), property substituted after the beginning of such 4 month period for property held as security at the time of such substitution shall, to the extent of the fair value of the property released, have the same status as the property released, and, to the

extent that any claim referred to in any of such paragraphs is created in renewal of or in substitution for or for the purpose of repaying or refunding any pre-existing claim of the Trustee as such creditor, such claim shall have the same status as such pre-existing claim.

If the Trustee shall be required to account, the funds and property held in such special account and the proceeds thereof shall be apportioned between the Trustee, the Securityholders and the holders of other indenture securities in such manner that the Trustee, the Securityholders and the holders of other indenture securities realize, as a result of payments from such special account and payments of dividends on claims filed against the obligor on the Securities in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, the same percentage of their respective claims, figured before crediting to the claim of the Trustee anything on account of the receipt by it from such obligor of the funds and property in such special account and before crediting to the respective claims of the Trustee and the Securityholders and the holders of other indenture securities dividends on claims filed against such obligor in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, but after crediting thereon receipts on account of the indebtedness represented by their respective claims from all sources other than from such dividends and from the funds and property so held in such special account. As used in this paragraph, with respect to any claim, the term "dividends" shall include any distribution with respect to such claim, in bankruptcy or receivership or proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, whether such distribution is made in cash, securities, or other property, but shall not include any such distribution with respect to the secured portion, if any, of such claim. The court in which such bankruptcy, receivership or proceedings for reorganization is pending shall have jurisdiction (i) to apportion between the Trustee and the Securityholders and the holders of other indenture securities, in accordance with the provisions of this paragraph, the funds and property held in such special account and proceeds thereof, or (ii) in lieu of such apportionment, in whole or in part, to give to the provisions of this paragraph due consideration in determining the fairness of the distributions to be made to the Trustee and the Securityholders and the holders of other indenture securities with respect to their respective claims, in which event it shall not be necessary to liquidate or to appraise the value of any securities or other property held in such special account or as security

for any such claim, or to make a specific allocation of such distributions as between the secured and unsecured portions of such claims, or otherwise to apply the provisions of this paragraph as a mathematical formula.

Any Trustee which has resigned or been removed after the beginning of such 4 month period shall be subject to the provisions of this Subsection as though such resignation or removal had not occurred. If any Trustee has resigned or been removed prior to the beginning of such 4 month period, it shall be subject to the provisions of this Subsection if and only if the following conditions exist:

(i) the receipt of property or reduction of claim, which would have given rise to the obligation to account if such Trustee had continued as Trustee, occurred after the beginning of such 4 month period; and

(ii) such receipt of property or reduction of claim occurred within 4 months after such resignation or removal.

(b) There shall be excluded from the operation of Subsection (a) of this Section a creditor relationship arising from

(1) the ownership or acquisition of securities issued under any indenture, or any security or securities having a maturity of one year or more at the time of acquisition by the Trustee;

(2) advances authorized by a receivership or bankruptcy court of competent jurisdiction, or by this Indenture, for the purpose of preserving any property which shall at any time be subject to the lien of this Indenture or of discharging tax liens or other prior liens or encumbrances thereon, if notice of such advances and of the circumstances surrounding the making thereof is given to the Securityholders at the time and in the manner provided in this Indenture;

(3) disbursements made in the ordinary course of business in the capacity of trustee under an indenture, transfer agent, registrar, custodian, paying agent, fiscal agent or depositary, or other similar capacity;

(4) an indebtedness created as a result of services rendered or premises rented; or an indebtedness created as a result of goods or securities sold in a cash transaction as defined in Subsection (c) of this Section;

(5) the ownership of stock or of other securities of a corporation organized under the provisions of Section 25(a) of the Federal Reserve Act, as amended, which is directly or indirectly a creditor of APS; or

(6) the acquisition, ownership, acceptance or negotiation of any drafts, bills of exchange, acceptances or obligations which fall within the classification of self-liquidating paper as defined in Subsection (c) of this Section.

(c) For the purposes of this Section only:

(1) The term "*default*" means any failure to make payment in full of the principal of or interest on any of the Securities or upon the other indenture securities when and as such principal or interest becomes due and payable;

(2) The term "*other indenture securities*" means securities upon which the Person obligated thereunder is an obligor (as defined in the Trust Indenture Act) outstanding under any other indenture (i) under which the Trustee is also trustee, (ii) which contains provisions substantially similar to the provisions of this Section, and (iii) under which a default exists at the time of the apportionment of the funds and property held in a special account as provided in Subsection (a) of this Section;

(3) The term "*cash transaction*" means any transaction in which full payment for goods or securities sold is made within 7 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;

(4) The term "*self-liquidating paper*" means any draft, bill of exchange, acceptance or obligation which is made, drawn, negotiated or incurred by any obligor on the Securities 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 such obligor arising from the making, drawing, negotiating or incurring of the draft, bill of exchange, acceptance or obligation;

(5) The term "*obligor*" means any obligor upon the Securities within the meaning of the TIA.

SECTION 9.14. *Maintenance of Agencies.*

(a) There shall at all times be maintained in the Borough of Manhattan, the City of New York, an office or agency where Securities may be presented or surrendered for transfer or exchange or for the registration thereof, and for payment of principal, premium (if any) and interest and where notices and demands to or upon the Trustee in respect of the Securities or of this Indenture may be served. Such office or agency shall be initially at the Paying Agent's Office. Written notice of the location of each such other office or agency and of any change of location thereof shall be given to the Company and to the Trustee. In the event that no such office or agency shall be maintained or no such notice of location or of change of location shall be given, presentations and demands may be made and notices may be served at the Corporate Trust Office.

(b) There shall at all times be a Security Registrar and a Paying Agent hereunder. Each such Authorized Agent shall be a bank or trust company, shall be a corporation organized and doing business under the laws of the United States or any State thereof, with a combined capital and surplus of at least \$50,000,000, and shall be authorized under such laws to exercise corporate trust powers, subject to supervision by Federal or State authorities. Chemical Bank, at its office specified in the first paragraph of this Indenture, is hereby appointed as Paying Agent and Security Registrar hereunder.

(c) Any Paying Agent (other than the Trustee) from time to time appointed hereunder shall execute and deliver to the Trustee an instrument in which said Paying Agent shall agree with the Trustee, subject to the provisions of this Section, that such Paying Agent will

(1) hold all sums held by it for the payment of principal of, and premium (if any) and interest on 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;

(2) give the Trustee within five days thereafter notice of any default by any obligor upon the Securities in the making of any such payment of principal, premium (if any) or interest; and

(3) at any time during the continuance of any such default, upon the written request of the Trustee, forthwith pay to the Trustee all sums so held in trust by such Paying Agent.

Notwithstanding any other provision of this Indenture, any payment required to be made to or received or held by the Trustee may, to the extent authorized by written instructions of the Trustee, be made to or received or held by a Paying Agent in the Borough of Manhattan, the City of New York, for the account of the Trustee.

(d) Any corporation into which any Authorized Agent may be merged or converted or with which it may be consolidated, or any corporation resulting from any merger, consolidation or conversion to which any Authorized Agent shall be a party, or any corporation succeeding to the corporate trust business of any Authorized Agent, shall be the successor of such Authorized Agent hereunder, if such successor corporation is otherwise eligible under this Section, without the execution or filing of any paper or any further act on the part of the parties hereto or such Authorized Agent or such successor corporation.

(e) Any Authorized Agent may at any time resign by giving written notice of resignation to the Trustee, APS and the Company. The Company may, and at the request of the Trustee or any Lessor shall, at any time, terminate the agency of any Authorized Agent by giving written notice of termination to such Authorized Agent and to the Trustee. Upon the resignation or termination of an Authorized Agent or in case at any time any such Authorized Agent shall cease to be eligible under this Section (when, in either case, no other Authorized Agent performing the functions of such Authorized Agent shall have been appointed), the Company shall promptly appoint one or more qualified successor Authorized Agents approved by the Trustee and each Lessor to perform the functions of the Authorized Agent which has resigned or whose agency has been terminated or who shall have ceased to be eligible under this Section. The Company shall give written notice of any such appointment to all Holders as their names and addresses appear on the Security Register.

ARTICLE TEN

SECURITYHOLDERS' LISTS AND REPORTS
BY TRUSTEE AND APSSECTION 10.01. *APS to Furnish Trustee Names and Addresses of Securityholders.*

APS will furnish or cause to be furnished to the Trustee semiannually, between January 15 and January 30, inclusive, and between July 15 and July 30, inclusive, in each year, and at such other times as the Trustee may request in writing, within 30 days after receipt by APS of any such request, a list, in such form as the Trustee may reasonably require, of the names and addresses of the Holders of Securities, in each case as of a date not more than 15 days prior to the time such list is furnished; provided, however, that so long as the Trustee is the sole Security Registrar, no such list need be furnished for so long as a copy of the Security Register is being furnished to the Trustee pursuant to Section 9.14(b).

SECTION 10.02. *Preservation of Information; Communications to Securityholders.*

(a) The Trustee shall preserve, in as current a form as is reasonably practicable, the names and addresses of Holders of Securities contained in the most recent list furnished to the Trustee as provided in Section 9.14(b) or Section 10.01, as the case may be, and the names and addresses of Holders of Securities received by the Trustee in its capacity as Security Registrar, if so acting. The Trustee may destroy any list furnished to it as provided in Section 9.14(b) or Section 10.01, as the case may be, upon receipt of a new list so furnished.

(b) If three or more Holders of Securities (hereinafter referred to as "applicants") apply in writing to the Trustee, and furnish to the Trustee reasonable proof that each such applicant has owned a Security for a period of at least six months preceding the date of such application, and such application states that the applicants desire to communicate with other Holders of Securities with respect to their rights under this Indenture or under the Securities and is accompanied by a copy of the form of proxy or other communication which such applicants propose to transmit, then the Trustee shall, within 5 Business Days after the receipt of such application, at its election, either:

(i) afford such applicants access to the information preserved at the time by the Trustee in accordance with Section 10.02(a), or

(ii) inform such applicants as to the approximate number of Holders of Securities whose names and addresses appear in the information preserved at the time by the Trustee in accordance with Section 10.02(a), and as to the approximate cost of mailing to such Securityholders the form of proxy or other communication, if any, specified in such application.

If the Trustee shall elect not to afford such applicants access to such information, the Trustee shall, upon the written request of such applicants, mail to each Securityholder whose name and address appear in the information preserved at the time by the Trustee in accordance with Section 10.02(a), a copy of the form of proxy or other communication which is specified in such request, with reasonable promptness after a tender to the Trustee of the material to be mailed and of payment, or provision for the payment, of the reasonable expenses of mailing, unless within five days after such tender, the Trustee shall mail to such applicants and file with the Commission, together with a copy of the material to be mailed, a written statement to the effect that, in the opinion of the Trustee, such mailing would be contrary to the best interests of the Holders of Securities or would be in violation of applicable law. Such written statement shall specify the basis of such opinions. If the Commission, after opportunity for a hearing upon the objections specified in the written statement so filed, shall enter an order refusing to sustain any of such objections or if, after the entry of an order sustaining one or more of such objections, the Commission shall find, after notice and opportunity for hearing, that all the objections so sustained have been met and shall enter an order so declaring, the Trustee shall mail copies of such material to all such Securityholders with reasonable promptness after the entry of such order and the renewal of such tender; otherwise the Trustee shall be relieved of any obligation or duty to such applicants respecting their application.

(c) Every Holder of Securities, by receiving and holding the same, agrees with APS and the Trustee that neither APS nor the Trustee shall be held accountable by reason of the disclosure of any such information as to the names and addresses of the Holders of Securities in accordance with Section 10.02(b), regardless of the source from which such information was derived, and that the Trustee shall not be held accountable by reason of mailing any material pursuant to a request made under Section 10.02(b).

SECTION 10.03. Reports by Trustee.

(a) Within 60 days after May 15 in each year, commencing with 1987, the Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, a brief report dated as of such May 15 with respect to:

(1) its eligibility under Section 9.09 and its qualifications under Section 9.08, or in lieu thereof, if to the best of its knowledge it has continued to be eligible and qualified under said Sections, a written statement to such effect;

(2) the character and amount of any advances (and if the Trustee elects so to state, the circumstances surrounding the making thereof) made by the Trustee (as such) which remain unpaid on the date of such report, and for the reimbursement of which it claims or may claim a lien or charge, prior to that of the Securities, on any property or funds held or collected by it as Trustee, except that the Trustee shall not be required (but may elect) to report such advances if such advances so remaining unpaid aggregate not more than $\frac{1}{2}$ of 1% of the principal amount of the Securities Outstanding on the date of such report;

(3) the amount, interest rate and maturity date of all other indebtedness owing by an obligor on the Securities within the meaning of the TIA to the Trustee in its individual capacity, on the date of such report, with a brief description of any property held as collateral security therefor, except an indebtedness based upon a creditor relationship arising in any manner described in Section 9.13(b) (2), (3), (4) or (6);

(4) the property and funds, if any, physically in the possession of the Trustee as such on the date of such report;

(5) any release, or release and substitution, of property subject to the lien of this Indenture (and the consideration therefor, if any) which the Trustee has not previously reported;

(6) any additional issue of Securities which the Trustee has not previously reported; and

(7) any action taken by the Trustee in the performance of its duties hereunder which it has not previously reported and which in its opinion materially affects the Securities, except action in respect of a

default, notice of which has been or is to be withheld by the Trustee in accordance with Section 9.02.

(b) The Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, a brief report with respect to:

(1) the release, or release and substitution, of property subject to the Lien of this Indenture (and the consideration therefor, if any), such report to be transmitted within 90 days of such time; and

(2) the character and amount of any advances (and if the Trustee elects so to state, the circumstances surrounding the making thereof) made by the Trustee (as such) since the date of the last report transmitted pursuant to Subsection (a) of this Section (or if no such report has yet been so transmitted, since the date of execution of this instrument) for the reimbursement of which it claims or may claim a lien or charge, prior to that of the Securities, on property or funds held or collected by it as Trustee, and which it has not previously reported pursuant to this Subsection, except that the Trustee shall not be required (but may elect) to report such advances if such advances remaining unpaid at any time aggregate 10% or less of the principal amount of the Securities Outstanding at such time, such report to be transmitted within 90 days after such time.

(c) A copy of each such report shall, at the time of such transmission to Securityholders, be filed by the Trustee with each stock exchange upon which the Securities are listed, and also with the Commission. APS will notify the Trustee when the Securities are listed on any stock exchange.

SECTION 10.04. Reports by APS.

APS will

(1) file with the Trustee, within 15 days after APS is required to file the same with the Commission, copies of the annual reports and of the information, documents and other reports (or copies of such portions of any of the foregoing as the Commission may from time to time by rules and regulations prescribe) which APS may be required to file with the Commission pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934; or, if APS is not required to file information, documents or reports pursuant to either of said Sections, then it will file with the Trustee and the Commission, in accordance

with rules and regulations prescribed from time to time by the Commission, such of the supplementary and periodic information, documents and reports which may be required pursuant to Section 13 of the Securities Exchange Act of 1934 in respect of a security listed and registered on a national securities exchange as may be prescribed from time to time in such rules and regulations;

(2) file with the Trustee and the Commission, in accordance with rules and regulations prescribed from time to time by the Commission, such additional information, documents and reports with respect to compliance by APS with the conditions and covenants of this Indenture as may be required from time to time by such rules and regulations; and

(3) transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, within 30 days after the filing thereof with the Trustee, such summaries of any information, documents and reports required to be filed by APS pursuant to paragraphs (1) and (2) of this Section as may be required by rules and regulations prescribed from time to time by the Commission.

ARTICLE ELEVEN

SUPPLEMENTAL INDENTURES

SECTION 11.01. *Supplemental Indentures Without Consent of Securityholders.*

Without the consent of the Holders of any Securities, APS, when authorized by a Board Resolution, the Company and the Trustee, at any time and from time to time, may enter into one or more indentures supplemental hereto (a "*Series Supplemental Indenture*" in the case of item 1 below), in form satisfactory to the Trustee, for any of the following purposes:

(1) to establish the form and terms of Securities of any series of Securities permitted by Sections 2.01 and 2.03; or

(2) to evidence the succession of another corporation to APS, and the assumption by any such successor of the covenants of APS herein contained, or to evidence the succession of another corporation to the

Company, and the assumption by any such successor of the covenants of the Company herein and in the Securities contained; or

(3) to add to the covenants of APS or the Company, for the benefit of the Holders of the Securities, or to surrender any right or power herein conferred upon APS or the Company; or

(4) to convey, transfer and assign to the Trustee, and to subject to the Lien of this Indenture, with the same force and effect as though included in the Granting Clauses hereof, additional Pledged Lessor Notes or additional properties or assets, and to correct or amplify the description of any property at any time subject to the Lien of this Indenture or to assure, convey and confirm unto the Trustee any property subject or required to be subject to the Lien of this Indenture; or

(5) to modify, eliminate or add to the provisions of this Indenture to such extent as shall be necessary to continue the qualification of this Indenture (including any supplemental indenture) under the TIA, or under any similar federal statute hereafter enacted, and to add to this Indenture such other provisions as may be expressly permitted by the TIA, excluding, however, the provisions referred to in Section 316(a)(2) of the TIA as in effect at the date as of which this instrument was executed or any corresponding provision in any similar federal statute hereafter enacted; or

(6) 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 provisions with respect to matters or questions arising under this Indenture, provided such action shall not adversely affect the interest of the Holders of the Securities.

SECTION 11.02. *Supplemental Indenture With Consent of Securityholders.*

With the consent of (i) the Holders of not less than a majority in principal amount of the Outstanding Securities, by Act of said Holders delivered to the Company and the Trustee, and (ii) APS, when authorized by a Board Resolution, and the Company may, and the Trustee, subject to Section 11.03, shall, enter into an indenture or indentures supplemental hereto for the purpose of adding any provisions to or changing in any manner the rights and obligations of the Holders of the Securities and of APS and the Company under this Indenture; *provided, however*, that no such supplemental indenture shall, without the consent of the Holder of each Outstanding Security affected thereby,

(1) change the Stated Maturity of the principal of, or any installment of interest on, or the dates or circumstances of payment of premium (if any) on, any Security, or reduce the principal amount thereof or the interest thereon or any premium payable upon the redemption thereof, or change the place of payment where, or the coin or currency in which, any Security or the premium (if any) or the interest thereon is payable, or impair the right to institute suit for the enforcement of any such payment of principal or interest on or after the Stated Maturity thereof (or, in the case of redemption, on or after the Redemption Date) or such payment of premium (if any) on or after the date such premium becomes due and payable or change the dates or the amounts of payments to be made through the operation of the Sinking Fund in respect of such Securities, or

(2) permit the creation of any lien prior to or, except with respect to additional series of Securities issued in accordance with the terms of this Indenture, *pari passu* with the Lien of this Indenture with respect to any of the Pledged Property, or terminate the Lien of this Indenture on any Pledged Property (except in each case as permitted by, and pursuant to, Article Four) or deprive any Securityholder of the security afforded by the Lien of this Indenture, or

(3) reduce the percentage in principal amount of the Outstanding Securities, the consent of whose Holders is required for any such supplemental indenture, or the consent of whose Holders is required for any waiver (of compliance with certain provisions of this Indenture or certain defaults hereunder and their consequences) provided for in this Indenture, or

(4) modify any of the provisions of this Section or Section 8.08, except to increase any such percentage or to provide that certain other provisions of this Indenture cannot be modified or waived without the consent of the Holder of each Security affected thereby.

Upon receipt by the Trustee of Board Resolutions of APS and the Company and such other documentation as the Trustee may reasonably require and upon the filing with the Trustee of evidence of the Act of said Holders, the Trustee shall join in the execution of such supplemental indenture or other instrument, as the case may be, subject to the provisions of Sections 11.03 and 11.04.

It shall not be necessary for any Act of Securityholders 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.

SECTION 11.03. *Documents Affecting Immunity or Indemnity.*

If in the opinion of the Company or the Trustee any document required to be executed by it pursuant to the terms of Section 11.02 affects any interest, right, duty, immunity or indemnity in favor of the Company or the Trustee under this Indenture or any of the Participation Agreements, the Company or the Trustee, as the case may be, may in its discretion decline to execute such document.

SECTION 11.04. *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 receive, and (subject to Section 9.01) 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.

SECTION 11.05. *Effect of Supplemental Indentures.*

Upon the execution 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.

SECTION 11.06. *Conformity with Trust Indenture Act.*

Every supplemental indenture executed pursuant to this Article shall conform to the requirements of the TIA as then in effect.

SECTION 11.07. *Reference in Securities to Supplemental Indentures.*

Securities authenticated and delivered after the execution of any supplemental indenture pursuant to this Article may, and shall if required by any Lessor or the Company, bear a notation in form approved by such Lessor, the Company and the Trustee as to any matter provided for in such supplemental indenture; and, in such case, suitable notation may be made upon Outstanding Securities after proper presentation and demand. If any Lessor or the Company shall so determine, new Securities so modified as to

conform, in the opinion of such Lessor, the Company and the Trustee, 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.

ARTICLE TWELVE

DEFEASANCE

SECTION 12.01. *Payment of Indebtedness; Satisfaction and Discharge of this Indenture.*

This Indenture shall cease to be of further effect (except as to any rights of registration of transfer or exchange of Securities herein expressly provided for and the rights of the Trustee, any predecessor Trustee and any Authorized Agent under Section 9.07), and the Trustee, on demand and at the expense of the Company, shall execute proper instruments acknowledging satisfaction and discharge of this Indenture, when

(1) either

(A) all Securities theretofore authenticated and delivered (other than (i) Securities which have been destroyed, lost or stolen and which have been replaced or redeemed as provided in Section 2.09 and (ii) Securities for the payment of which money held in trust hereunder has been paid to the Company and discharged from such trust, as provided in Section 5.03) have been delivered to the Trustee for cancellation; or

(B) all such Securities not theretofore delivered to the Trustee for cancellation

(i) have become due and payable, or

(ii) will become due and payable at their Stated Maturity of principal within one year, or

(iii) are to be called for redemption within one year under arrangements satisfactory to the Trustee for the giving of notice of redemption by the Trustee in the name and at the expense of the Company, and the Company, in the case of (i), (ii) or (iii) above, has deposited or caused to be deposited with the Trustee in trust (subject to Section 9.06 hereof) for the purpose of paying and discharging the entire indebted-

ness on such Securities not theretofore cancelled by the Trustee or delivered to the Trustee for cancellation, an amount sufficient to discharge such indebtedness, including principal, premium (if any) and interest to the date of such deposit (in the case of Securities which have become due and payable), or to the Stated Maturity of principal or Redemption Date, as the case may be;

(2) All other sums then due and payable hereunder have been paid; and

(3) APS or the Company has delivered to the Trustee an Officers' Certificate and an Opinion of Counsel each stating that all conditions precedent herein provided for relating to the satisfaction and discharge of this Indenture have been complied with.

SECTION 12.02. *Application of Deposited Money.*

All money deposited with the Trustee pursuant to Section 12.01 shall be held in trust and applied by it, in accordance with the provisions of the Securities and this Indenture, to the payment to the Persons entitled thereto of the principal, premium (if any), and interest for the payment of which such money has been deposited with the Trustee.

ARTICLE THIRTEEN

RELEASE OF FUNDS BY THE TRUSTEE FOR PAYMENT OF THE PLEDGED LESSOR NOTES AND RELEASE AND SUBSTITUTION OF PLEDGED PROPERTY

SECTION 13.01. *Conditions Precedent to Release of Funds by the Trustee for Payment of the Pledged Lessor Notes.*

The obligation of the Trustee to make payments to the Lessors pursuant to Section 2.15(b) hereof is subject to the receipt by the Trustee of the following:

(a) an executed counterpart of a supplemental indenture appropriate to subject to the Lien of this Indenture the related Pledged Lessor Notes;

(b) the documents, opinions and certificates specified in the proviso to Section 2.04;

(c) a certificate of each Lessor dated as of the Closing Date under the related Participation Agreement (i) specifying the principal amount of the Pledged Lessor Note to be issued thereby and (ii) stating that (A) such Lessor has received the amount of the Equity Participant's investment pursuant to applicable provisions of such Participation Agreement and that such amount is available for use by such Lessor pursuant to applicable provisions of such Participation Agreement upon receipt of the amount to be paid by the Trustee with respect to such Pledged Lessor Note pursuant to Section 2.15(b) hereof; (B) to the best knowledge of such Lessor no event has occurred and is continuing which constitutes an Indenture Event of Default, or would constitute an Indenture Event of Default after notice or lapse of time or both under the related Lease Indenture and (C) the Pledged Lessor Note of such Lessor has been duly authorized, executed and delivered by such Lessor and is a valid and binding obligation of such Lessor; and

(d) such other documents and evidence with respect to the Lessors and the Company as the Trustee may reasonably request.

This instrument may be executed in any number of counterparts, each of which when so executed shall be deemed to be an original, but all such counterparts shall together constitute but one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this Indenture to be duly executed, and their respective corporate seals to be hereunto affixed and attested, all as of the day and year first above written. -

PVNGS FUNDING CORP., INC.

By /s/ PETER FARLEY
Vice President

Attest:

/s/ RICHARD FRANZEN
Assistant Secretary

ARIZONA PUBLIC SERVICE COMPANY

By /s/ P. A. WILLIAMS
Vice President and Treasurer

Attest:

/s/ FAYE WIDENMANN
Secretary

CHEMICAL BANK

By /s/ T. J. FOLEY
Vice President

Attest:

/s/ G. McFARLANE
Trust Officer

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On this 19th day of November, 1986, before me personally came Peter C. Farley, to me known, who, being by me duly sworn, did depose and say that he resides at Wilmington, Delaware; that he is the Vice President of PVNGS FUNDING CORP., INC., one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693465
Qualified in New York County
Commission Expires March 30, 1987

[NOTARIAL SEAL]

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On this 19th day of November, 1986, before me personally came Paul A. Williams II, to me known, who, being by me duly sworn, did depose and say that he resides at Phoenix, Arizona; that he is the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693168
Qualified in New York County
Commission Expires March 30, 1987

[NOTARIAL SEAL]

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On the 19th day of November, 1986, before me personally came T. J. Foley, to me known who, being by me duly sworn, did depose and say that he resides at Bethpage, New York; that he is a Vice-President of CHEMICAL BANK, a New York banking corporation and one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation, and that he signed his name thereto on behalf of said corporation by like order.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693465
Qualified in New York County
Commission Expires March 30, 1987

[NOTARIAL SEAL]

EXHIBIT A
TO
COLLATERAL TRUST INDENTURE

REQUIREMENTS FOR PLEDGED LESSOR
NOTES AND LEASE INDENTURES

The Pledged Lessor Notes and the Lease Indentures relating to any series of Securities shall contain the provisions summarized below or other provisions substantially as protective or more protective of the interests of Holders of Outstanding Securities. Notwithstanding the foregoing, (i) the Principal Instruments in connection with the initial series of Securities issued under this Indenture shall be deemed to satisfy all criteria set forth in this Exhibit A and (ii) the Principal Instruments in connection with any subsequent series of Securities, if substantially similar in form and substance to the Principal Instruments in connection with such initial series of Securities, shall also be deemed to satisfy all criteria set forth in this Exhibit A.

I. Each Pledged Lessor Note will:

(i) be duly issued pursuant to, and be secured by, the related Lease Indenture;

(ii) provide for the payment to the registered holder thereof, not later than when due, of amounts at least equal to that portion of all principal of and premium, if any, and interest on the series of Securities issued in connection with and relating to the pledge thereof under the Indenture, such payment to be without defenses or set-offs and otherwise unconditional;

(iii) (A) if such Pledged Lessor Note is the initial series issued under the related Lease Indenture, the principal amount thereof shall not exceed an amount equal to 80% of the sum of the aggregate purchase price of the property being purchased with the proceeds of the issuance and sale of such Lessor Note; and (B) if such Pledged Lessor Note is of an additional series issued under the related Lease Indenture, the sum of the principal amount thereof and the principal amount of Pledged Lessor Notes theretofore issued under such Lease Indenture shall not exceed an amount equal to 80% of the sum of (1)

the aggregate purchase price of property being purchased with the proceeds of the issuance and sale of such Lessor Note and (2) the aggregate purchase price of the property purchased with the proceeds of the issuance and sale of each Pledged Lessor Note theretofore issued; and

(iv) provide that no Change to the Pledged Lessor Note may be made without the consent of the holder thereof.

II. Each Lease Indenture will:

(i) assign to the Lease Indenture Trustee obligations under the related Lease to which the Owner Trustee then or thereafter is entitled at least sufficient to pay the principal of, premium, if any, and interest on the related Pledged Lessor Note; and

(ii) contain provisions no less protective of the interests of Holders of Securities than the following provisions of the Lease Indentures in connection with the initial series of Securities: Article II, Sections 3.4, 3.5, 3.6, 3.8, 3.11, Article V, Article VI and Article VII.

PVNGS FUNDING CORP., INC.,

ARIZONA PUBLIC SERVICE COMPANY

and

CHEMICAL BANK,
as Trustee

SERIES 1986 BOND SUPPLEMENTAL INDENTURE

dated as of November 15, 1986

to

COLLATERAL TRUST INDENTURE

dated as of November 1, 1986

Providing for the Issuance of
\$273,000,000 Aggregate Principal Amount
of Secured Lease Obligation Bonds, Series 1986
with the Interest Rates and Stated Maturities
Set Forth Herein

PALO VERDE NUCLEAR GENERATING STATION

WHEREAS, the Bonds to be issued hereunder are to be substantially in the form annexed as Schedule.1 hereto; and

WHEREAS, all acts and things necessary to make the Bonds, when executed by the Company and authenticated and delivered by the Trustee as provided in the Original Indenture, the valid, binding and legal obligations of the Company, and to constitute these presents a valid and binding supplemental indenture and agreement according to its terms, have been done and performed, and the execution of this Series 1986 Bond Supplemental Indenture and the creation and issuance under the Indenture of \$273,000,000 aggregate principal amount of the Bonds have in all respects been duly authorized, and the Company, in the exercise of legal right and power in it vested, executes this Series 1986 Bond Supplemental Indenture and proposes to create, execute, issue and deliver the Bonds:

NOW, THEREFORE, THIS SERIES 1986 BOND SUPPLEMENTAL INDENTURE WITNESSETH:

That in order to establish the form and terms of and to authorize the authentication and delivery of the Bonds, and in consideration of the acceptance of the Bonds by the holders thereof and of the sum of one dollar duly paid to the Company by the Trustee at the execution of these presents, the receipt whereof is hereby acknowledged, the Company and APS each covenant and agree with the Trustee, for the equal and proportionate benefit of the respective holders from time to time of the Bonds, as follows:

ARTICLE ONE

THE BONDS

SECTION 1.01. Terms of the Bonds.

There is hereby created a series of Securities designated "Secured Lease Obligation Bonds, Series 1986". Bonds in the aggregate principal amount of \$273,000,000 may forthwith be executed by the Company and delivered to the Trustee for authentication and delivery by the Trustee in accordance with the provisions of Section 2.04 of the Original Indenture in the following amounts for the Stated Maturities of principal and at the interest rates indicated:

<u>Stated Maturity of Principal</u>	<u>Interest Rate</u>	<u>Principal Amount</u>
December 30, 1998	9%	\$ 35,184,000
June 30, 2015	10.45%	237,816,000
		<hr/> \$273,000,000

The Bonds shall be payable, bear interest and have and be subject to such other terms as provided in the form of Bond attached as Schedule 1 hereto.

SECTION 1.02. Mandatory Redemption of the Bonds.

(a) Termination of Lease. In the event that there shall occur under Section 14 of any Lease identified in Schedule 2 hereto a termination of such Lease, Bonds shall be redeemed, in part, in proportion to the principal amount of the Pledged Lessor Notes related to such Lease (the Prepaid Lessor Notes) prepaid in accordance with their terms and Section 5.2 of the Lease Indenture under which such Pledged Lessor Notes are issued. Any such redemption shall be on the date set

forth in the redemption notice delivered by the Trustee pursuant to Section 1.02(b) of this Series 1986 Bond Supplemental Indenture and shall be made to the extent that the Prepaid Lessor Notes are so prepaid, together with accrued interest thereon.

(b) Notice of Redemption and Redemption Date. Redemption of Bonds pursuant to Section 1.02(a) of this Series 1986 Bond Supplemental Indenture shall be on the Redemption Date set forth in the redemption notice delivered by the Trustee pursuant to Section 6.03 of the Original Indenture, which Redemption Date shall correspond to the Obsolescence Redemption Date following the Termination Date specified in the Termination Notice received by the Trustee relating to the Prepaid Lessor Notes.

(c) Selection. Any Bonds redeemed pursuant to Section 1.02(a) of this Series 1986 Bond Supplemental Indenture shall be selected in accordance with Section 6.02 of the Original Indenture, but without giving effect to the proviso contained in such Section.

(d) Redemption Price. The Redemption Price for any Bond to be redeemed pursuant to this Section 1.02 shall be 100% of the principal amount thereof, together with accrued interest to the Redemption Date.

SECTION 1.03. Optional Redemption of Bonds.

The Bonds shall be redeemable prior to maturity at the option of the Company at the times and redemption prices set forth in the form of Bond attached as Schedule 1 hereto.

SECTION 1.04. Sinking Fund.

(a) Amounts and Dates. The Bonds shall be redeemed through operation of a sinking fund. The amount of each Sinking Fund payment (subject to adjustment as provided in paragraph (b) below) and each

Sinking Fund Date applicable to a Stated Maturity of principal of the Bonds are as set forth below:

Sinking Fund Date	Stated Maturity	
	December 30, 1998	June 30, 2015
December 30, 1989	\$ 65,000	-
June 30, 1990	495,000	-
December 30, 1990	978,000	-
June 30, 1991	1,022,000	-
December 30, 1991	1,068,000	-
June 30, 1992	1,116,000	-
December 30, 1992	1,166,000	-
June 30, 1993	1,218,000	-
December 30, 1993	1,273,000	-
June 30, 1994	1,330,000	-
December 30, 1994	1,391,000	-
June 30, 1995	1,454,000	-
December 30, 1995	1,518,000	-
June 30, 1996	1,587,000	-
December 30, 1996	1,658,000	-
June 30, 1997	1,733,000	-
December 30, 1997	5,136,000	-
June 30, 1998	5,367,000	-
December 30, 1998	5,609,000	-
June 30, 1999		\$ 3,485,000
December 30, 1999		4,722,000
June 30, 2000		5,169,000
December 30, 2000		5,148,000
June 30, 2001		5,147,000
December 30, 2001		4,558,000
June 30, 2002		4,979,000
December 30, 2002		4,862,000
June 30, 2003		5,313,000
December 30, 2003		5,187,000
June 30, 2004		5,533,000
December 30, 2004		5,392,000
June 30, 2005		5,856,000
December 30, 2005		5,704,000
June 30, 2006		6,250,000

Sinking Fund Date	Stated Maturity	
	December 30, 1998	June 30, 2015
December 30, 2006		6,086,000
June 30, 2007		6,670,000
December 30, 2007		6,493,000
June 30, 2008		7,118,000
December 30, 2008		6,928,000
June 30, 2009		7,596,000
December 30, 2009		7,393,000
June 30, 2010		8,107,000
December 30, 2010		7,888,000
June 30, 2011		8,652,000
December 30, 2011		8,417,000
June 30, 2012		9,234,000
December 30, 2012		10,279,000
June 30, 2013		9,751,000
December 30, 2013		11,616,000
June 30, 2014		14,316,000
December 30, 2014		17,035,000
June 30, 2015		6,932,000

(b) Certain Adjustments to Sinking Funds.

The principal amount of Bonds of a particular Stated Maturity of principal to be redeemed through operation of the Sinking Fund for the Bonds of such Stated Maturity of principal may be adjusted once (upward or downward) at the discretion of the Company (contemporaneously with similar adjustments for all Stated Maturities of principal) prior to June 30, 1989; provided, however, that no such adjustment shall be made by the Company which will increase or reduce the average life of the Bonds of such Stated Maturity of principal (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than 6 months; provided further, however, such adjustment may only be made in connection with an adjustment to basic rent pursuant to Section 3(d) of one or more of the Leases identified in Schedule 2 hereto. If the Company shall elect to make the foregoing adjustment, the Company shall deliver to the Trustee and APS at

least 60 days prior to the first Sinking Fund Date proposed to be affected by such adjustment, a Company Request (w) stating that the Company has elected to make such adjustment in connection with adjustments to basic rent under one or more of such Leases, (x) setting forth a revised schedule of principal amounts of the Sinking Fund applicable to Bonds of the affected Stated Maturity of principal, (y) attaching a copy of the revised schedules of principal amortization for the related Pledged Lessor Notes identified in Schedule 2 hereto, and (z) attaching calculations showing that (i) the average life of the Bonds of the affected Stated Maturity of principal will not be reduced or increased except as permitted by this paragraph (b), (ii) the aggregate principal amount of the Pledged Lessor Notes identified on Schedule 2 hereto equals the aggregate principal amount of the Bonds and (iii) the aggregate amortization of the principal amount of such Pledged Lessor Notes is sufficient to repay in full, as and when due, the principal amount of the Bonds as and when due, whether upon redemption through operation of the applicable Sinking Funds or at maturity. The Trustee may rely on such Company Request and shall have no duty with respect to the calculations referred to in the foregoing clause (z), other than to make them available for inspection by any Holder of Bonds at the Corporate Trust Office upon reasonable notice. The Trustee shall, at the expense of APS, send to each Holder of Bonds of the affected Stated Maturity of principal at least 20 days before the first Sinking Fund Date to be affected thereby, by first class mail, a copy of such revised schedule of principal amounts of Sinking Fund payments applicable to such Bonds.

(c) Redemption Price. The Redemption Price for any Bond to be redeemed pursuant to paragraph (a) of this Section 1.04 shall be 100% of the principal amount thereof, together with accrued interest to the Redemption Date.

ARTICLE TWO

PLEDGE OF LESSOR NOTES

To secure the payment of the principal of, and premium, if any, and interest, on all the Securities from time to time Outstanding under the Indenture, and the performance of the covenants therein and herein contained, the Company by these presents does grant, bargain, sell, release, convey, assign, transfer, mortgage, hypothecate, pledge, confirm and create a security interest in, unto the Trustee, the Lessor Notes identified on Schedule 2 hereto (herein referred to as the Pledged Lessor Notes).

TO HAVE AND TO HOLD the aforesaid Pledged Lessor Notes unto the Trustee and its successors and assigns forever, in trust and for the uses and purposes and subject to the covenants and conditions set forth in the Indenture.

ARTICLE THREE

MISCELLANEOUS

SECTION 3.01. Execution as Supplemental Indenture.

This Series 1986 Bond Supplemental Indenture is executed and shall be construed as an indenture supplemental to the Original Indenture and, as provided in the Original Indenture, this Series 1986 Bond Supplemental Indenture forms a part thereof. Except as expressly otherwise defined herein or in Schedule 2 hereof, the use of the terms herein is in accordance with the definitions contained in the Original Indenture.

SECTION 3.02. Responsibility for Recitals,
Etc.

The recitals contained herein and in the Bonds, except the Trustee's certificate of authentication, shall be taken as the statements of the Company and APS, and the Trustee assumes no responsibility for the correctness of the same. The Trustee makes no representation as to the validity or sufficiency of this Series 1986 Bond Supplemental Indenture or the Bonds.

SECTION 3.03. Provisions Binding on
Successors.

All the covenants, stipulations, promises and agreements in this Series 1986 Bond Supplemental Indenture contained by or on behalf of the Company shall bind its successors and assigns, whether so expressed or not.

SECTION 3.04. New York Contract.

This Series 1986 Bond Supplemental Indenture and each Bond shall be deemed to be a contract under the laws of the State of New York, and for all purposes shall be governed by and construed in accordance with the laws of said state.

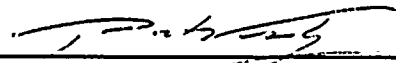
SECTION 3.05. Counterparts.

This Series 1986 Bond Supplemental Indenture may be executed in any number of counterparts, each of which shall be an original; but such counterparts shall together constitute but one and the same instrument.

IN WITNESS WHEREOF, the Company, APS and the Trustee have caused this Series 1986 Bond Supplemental Indenture to be duly executed by their respective officers thereunto duly authorized, as of the date and year first above written.

PVNGS FUNDING CORP., INC.

[CORPORATE SEAL]

By 
Vice President

Attest:


Assistant Secretary

ARIZONA PUBLIC SERVICE
COMPANY

[CORPORATE SEAL]

By 
Vice President and Treasurer

Attest:


Assistant Secretary

CHEMICAL BANK,
as Trustee,

[CORPORATE SEAL]

By


Vice President

Attest:


Trust Officer

STATE OF NEW YORK)

: SS.:

COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came Peter C. Farley, to me known, who, being by me duly sworn, did depose and say that he resides at Wilmington, Delaware; that he is the Vice President of PVNGS FUNDING CORP., INC., one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693458
Qualified in New York County
Commission Expires March 30, 1993 7

STATE OF NEW YORK)
 : SS.:
COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came Paul A. Williams II, to me known, who, being by me duly sworn, did depose and say that he resides at Phoenix, Arizona; that he is the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693468
Qualified in New York County
Commission Expires March 30, 1987

STATE OF NEW YORK)

: ss.:

COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came T.J. Foley, to me known, who, being by me duly sworn, did depose and say that he resides at Bethpage, New York; that he is Vice President of CHEMICAL BANK, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693468
Qualified in New York County
Commission Expires March 30, 1987 7

SCHEDULE 1
to
SERIES 1986 BOND
SUPPLEMENTAL INDENTURE

[FORM OF FACE OF BOND]

No. R-

\$ _____

PVNGS FUNDING CORP., INC.

SECURED LEASE OBLIGATION BOND SERIES 1986

INTEREST RATE	STATED MATURITY	ISSUE DATE	CUSIP
---------------	-----------------	------------	-------

Registered
Holder:

Principal
Amount: Dollars

PVNGS FUNDING CORP., INC., a Delaware corporation (herein called the "Company", which term includes any successor corporation under the Indenture referred to on the reverse hereof), for value received, hereby promises to pay to the Registered Holder hereof, or registered assigns, the Principal Amount (stated above) on the Stated Maturity (stated above) and to pay interest thereon from the date hereof, or from the most recent interest payment date to which interest has been paid or duly provided for, semiannually on June 30 and December 30, in each year, commencing December 30, 1986, at the Interest Rate (stated above) per annum, until the principal hereof is paid in full or made available for payment. The interest so payable, and punctually paid or duly provided for, on any interest payment date will,

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as provided in such Indenture, be paid to the person in whose name this Bond (or one or more Predecessor Securities, as defined in such Indenture) is registered at the close of business on the Regular Record Date (as defined in such Indenture) for such interest, which shall be the June 15 or December 15, as the case may be (whether or not a Business Day, as defined in such Indenture), next preceding such interest payment date. Any such interest not so punctually paid or duly provided for shall forthwith cease to be payable to the Registered Holder on such Regular Record Date, and may be paid to the person in whose name this Bond (or one or more Predecessor Securities) is registered at the close of business on a Special Record Date (as defined in such Indenture) for the payment of such defaulted interest to be fixed by the Trustee, notice of which shall be given to the Bondholders not less than 10 days prior to such Special Record Date, or may be paid at any time in any other lawful manner not inconsistent with the requirements of any securities exchange on which the Bonds may be listed, and upon such notice as may be required by such exchange, all as more fully provided in such Indenture. Payment of the principal of, and premium, if any, and interest on, this Bond will be made at the Corporate Trust Office of the Trustee (or if such office is not in the Borough of Manhattan, The City of New York, at either such office or an office to be maintained in such Borough), in such coin or currency of the United States of America as at the time of payment is legal tender for payment of interest or may be made at the option of the Company by check mailed to the address of the Holder entitled thereto as such address shall appear on the Security Register.

Reference is hereby made to the further provisions of this Bond set forth on the reverse hereof which further provisions shall for all purposes have the same effect as if set forth at this place.

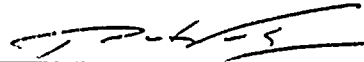
Unless the certificate of authentication hereon has been executed by the Trustee by manual signature, this Bond shall not be entitled to any

benefit under such Indenture, or be valid or obligatory for any purpose.

IN WITNESS WHEREOF, the Company has caused this instrument to be duly executed under its corporate seal.

PVNGS FUNDING CORP., INC.

By



Vice President

Attest:



Assistant Secretary

[FORM OF CERTIFICATE OF AUTHENTICATION]

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

CHEMICAL BANK,
as Trustee

By

Authorized Officer

[FORM OF REVERSE OF BOND]

PVNGS FUNDING CORP., INC.

SECURED LEASE OBLIGATION BOND, SERIES 1986

This Bond is one of an authorized issue of Securities of the Company known as its "Secured Lease Obligation Bonds, Series 1986" (the "Bonds"). The Bonds are issued under and secured by a Collateral Trust Indenture dated as of November 1, 1986 among the Company, Arizona Public Service Company, an Arizona corporation (herein called "APS"), and Chemical Bank, as Trustee (herein called the "Trustee", which term includes any successor Trustee under the Indenture), as supplemented by the Series 1986 Bond Supplemental Indenture dated as of November 15, 1986 among such parties (collectively, the "Indenture"). All Bonds are secured equally and ratably with one another and with any other Securities of the Company issued under the Indenture, as amended or supplemented. Reference is hereby made to the Indenture for a description of the nature and extent of the securities and other property assigned, pledged and transferred thereunder, the respective rights of the holders of the Bonds and of the Trustee and the Company in respect of such security, and the terms upon which the Bonds are and are to be authenticated and delivered.

The principal of, and premium, if any, and interest on, this Bond are payable from, and secured by, the assets subject to the lien of the Indenture and the income and proceeds received by the Trustee therefrom, and all payments of principal, and premium, if any, and interest shall be made in accordance with the terms of the Indenture.

The Indenture provides that certain nonrecourse promissory notes ("Pledged Lessor Notes") are subject to the lien of the Indenture and that additional Pledged Lessor Notes, as and when issued, can be made subject to the lien of the Indenture pursuant to indenture supplements. The Pledged Lessor Notes subject

to the lien of the Indenture on the date of the initial issuance of Bonds were issued by The First National Bank of Boston, as owner trustee under two separate Trust Agreements with the respective institutional investors named in such Trust Agreements. Such Pledged Lessor Notes were issued under separate documents entitled Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, each between an owner trustee, as lessor, and Chemical Bank, as trustee (each of such Trust Indentures, as it was executed and delivered and as thereafter amended in accordance with its terms, and any similar instruments pursuant to which additional Pledged Lessor Notes are issued, being herein called a "Lease Indenture", each trustee thereunder being herein called a "Lease Indenture Trustee" and each lessor thereunder being herein called a "Lessor"). Reference is made to each Lease Indenture for a description of the nature and extent of property assigned, pledged, transferred and mortgaged thereunder and the rights of the holders of Pledged Lessor Notes. Except as expressly provided in a Lease Indenture, all payments of principal, and premium, if any, and interest to be made on a Pledged Lessor Note issued under such Lease Indenture will be made only from the assets subject to the lien of such Lease Indenture or the income and proceeds received by the Lease Indenture Trustee therefrom, including, in the case of each Lease Indenture, the rights of the Lessor which is a party thereto to receive basic rentals and certain other payments under a Lease with APS relating to an undivided interest in certain assets constituting part of the Palo Verde Nuclear Generating Station (also known as the Arizona Nuclear Power Project) (each of such Leases, as it is executed and delivered and as thereafter amended in accordance with its terms being herein called a "Lease"), which basic rentals and other payments will be at least sufficient to provide for the payment of the principal of, and premium, if any, and interest on, each Pledged Lessor Note issued under such Lease Indenture. Each Holder hereof, by its acceptance of this Bond, agrees (x) that except as expressly provided above, it will look solely to the assets subject to the lien of the Indenture or the income and proceeds received by the

Trustee therefrom, to the extent available for distribution to the Holder hereof as provided in the Indenture and (y) that none of any institutional investor which is a party to a Trust Agreement (an "Equity Participant"), any Lessor, any Lease Indenture Trustee or the Trustee is liable to the Holder hereof or, in the case of an Equity Participant, any Lessor and any Lease Indenture Trustee, to the Trustee for any amounts payable under this Bond or, except as provided in the Indenture with respect to the Trustee, for any liability under the Indenture. An Equity Participant shall not have any duty or responsibility under the Indenture or the Bonds to any Holder or to the Trustee.

The Indenture permits, with certain exceptions as therein provided, the amendment thereof and the modification of the rights and obligations of APS and the Company and the rights of the Holders of the Securities under the Indenture at any time by APS and the Company with the consent of the Holders of not less than a majority in aggregate principal amount of the Securities at the time Outstanding, as defined in the Indenture. The Indenture also contains provisions permitting the Holders of specified percentages in aggregate principal amount of the Securities at the time Outstanding, on behalf of the Holders of all the Securities, to waive compliance by APS and 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 Bond shall be conclusive and binding upon such Holder and upon all future Holders of this Bond and of any Security issued upon the transfer hereof or in exchange herefor or in lieu hereof whether or not notation of such consent or waiver is made upon this Bond.

As provided in the Indenture, the aggregate principal amount of Securities which may be issued thereunder is unlimited. The Bonds are limited in aggregate principal amount to \$273,000,000, consisting of:

<u>Stated Maturity of Principal</u>	<u>Interest Rate</u>	<u>Principal Amount</u>
December 30, 1998	9.00%	\$ 35,184,000
June 30, 2015	10.45%	237,816,000
		<u>\$273,000,000</u>

In the event that one or more Leases are terminated under Section 14 thereof, the Bonds are subject to mandatory redemption in whole or in part in proportion to the principal amount of Pledged Lessor Notes related to such Lease or Leases prepaid in accordance with their terms and Section 5.2 of the Lease Indenture or Lease Indentures under which such Pledged Lessor Notes were issued. Any such redemption shall be on not less than 20 nor more than 60 days' prior notice given as provided in Section 6.03 of the Indenture and Section 1.02(b) of the Series 1986 Bond Supplemental Indenture at a redemption price equal to the principal amount of the Bonds to be redeemed plus accrued interest to the date fixed for redemption, to the extent that the Pledged Lessor Notes relating to the Bonds are prepaid.

The Bonds of each Stated Maturity of principal are also subject to mandatory redemption pursuant to sinking fund installments, as more fully provided in the Indenture, at the principal amount thereof, together with interest accrued to the date fixed for redemption, on the dates and in the respective principal amounts set forth in the Indenture.

The sinking fund installments for the Bonds of a particular Stated Maturity of principal may be adjusted once at the discretion of the Company prior to June 30, 1989, in connection with certain adjustments in basic rent pursuant to any of the Leases.

In the event of any partial redemption of Bonds of a particular Stated Maturity of principal (other than pursuant to the aforementioned sinking fund), the principal amount of Bonds of such Stated Maturity of principal to be redeemed thereafter pursuant to the sinking fund schedule indicated in the Indenture shall be adjusted proportionately as nearly as practicable in accordance with Section 7.01 of the Indenture.

In addition, the Bonds are subject to redemption, in whole or in part, at any time, at the option of the Company, with monies deposited with the Trustee, on not less than 20 nor more than 60 days' notice given as provided in the Indenture, at the following redemption prices (expressed as a percentage of principal amount), together with interest accrued to the date fixed for redemption as follows:

Bonds with a Stated Maturity of principal of December 30, 1998 may be redeemed at the following redemption prices (expressed as a percentage of principal amount), together with interest accrued to the Redemption Date:

<u>If Redeemed During the Twelve Months Beginning December 30,</u>	<u>Redemption Price</u>
1991	104.50%
1992	103.60
1993	102.70
1994	101.80
1995	100.90

and thereafter at the principal amount thereof, together with interest accrued to the Redemption Date; and

Bonds with a Stated Maturity of principal of June 30, 2015 may be redeemed at the following

redemption prices (expressed as a percentage of principal amount), together with interest accrued to the Redemption Date:

<u>If Redeemed During the Twelve Months Beginning December 30,</u>	<u>Redemption Price</u>
1991	107.70%
1992	107.15-
1993	106.60
1994	106.05
1995	105.50
1996	104.95
1997	104.40
1998	103.85
1999	103.30
2000	102.75
2001	102.20
2002	101.65
2003	101.10
2004	100.55

and thereafter at the principal amount thereof, together with interest accrued to the Redemption Date.

In the case of any redemption of Bonds, unpaid interest installments whose Stated Maturity, as defined in the Indenture, is on or prior to the date fixed for redemption will be payable to the Holders of such Bonds or one or more Predecessor Securities of record at the close of business on the relevant Regular or Special Record Date referred to on the face hereof.

Bonds (or portions thereof as aforesaid) for which redemption and payment provision is made in accordance with the Indenture shall thereupon cease to be entitled to the lien of the Indenture and shall cease to bear interest from and after the date fixed for redemption.

If an Event of Default, as defined in the Indenture, shall occur, the principal of this Bond may become or be declared due and payable, in the manner and with the effect provided in the Indenture.

This Bond is transferable by the registered owner hereof in person or by attorney authorized in writing, at the corporate trust office of the Bond Registrar, Chemical Bank (or if such office is not in the Borough of Manhattan, The City of New York, at either such office or an office to be maintained in such Borough), upon surrender of this Bond, and upon any such transfer a new Bond of the same Stated Maturity of principal, for the same aggregate principal amount, will be issued to the transferee in exchange herefor.

The Bonds are issuable only as registered Bonds without coupons in denominations of \$1,000 and/or any integral multiple thereof. As provided in, and subject to the provisions of, the Indenture, Bonds of a particular Stated Maturity of principal are exchangeable for other Bonds of such Stated Maturity, but of a different authorized denomination or denominations, as requested by the Holder surrendering the same.

No service charge will be made to any Holder of Bonds for any such transfer or exchange, but the Bond Registrar may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith.

Prior to due presentment for registration of transfer, the person in whose name this Bond is registered shall be deemed to be the owner hereof for the purpose of receiving payment as herein provided and for all other purposes whether or not this Bond be overdue, regardless of any notice to anyone to the contrary.

All capitalized terms used herein, unless defined herein, shall have the meanings ascribed to them in the Indenture.

As provided in the Indenture, the Indenture and the Bonds shall be construed in accordance with and governed by the law of the State of New York:

SCHEDULE 2
to
SERIES 1986 BOND
SUPPLEMENTAL INDENTURE

A. As used in this Series 1986 Bond Supplemental Indenture, the following terms have the following meanings:

(1) Lease Indenture means each of:

(i) the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Indenture Trustee and the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation, as amended by Supplemental Indenture No. 1 thereto, dated as of November 1, 1986; and

(ii) the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Indenture Trustee and the Owner Trustee, as owner trustee for Emerson Capital Corporation, successor to Emerson Finance Co., as amended by Supplemental Indenture No. 1 thereto, dated as of November 1, 1986.

(2) Lessor Note means each of:

(i) the Non-Recourse Promissory Note, Refunding Series (Due December 30, 1998) in the amount of \$14,228,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation to the Company;

(ii) the Non-Recourse Promissory Note, Refunding Series (Due June 30, 2015) in the amount of \$98,772,000 dated

November 19, 1986, payable by the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation to the Company;

(iii) the Non-Recourse Promissory Note, Refunding Series (Due December 30, 1998) in the amount of \$20,956,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Emerson Capital Corporation to the Company; and

(iv) the Non-Recourse Promissory Note, Refunding Series (Due June 30, 2015) in the amount of \$139,044,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Emerson Capital Corporation to the Company.

(3) Lessor or Owner Trustee means The First National Bank of Boston, a national banking association (FNB), in its capacity as owner trustee under two separate Trust Agreements, each dated as of August 1, 1986, with the Equity Participant named therein.

(4) Indenture Trustee means Chemical Bank, a New York banking corporation, as Trustee.

(5) Lease means each of:

(i) the Facility Lease, dated as of August 1, 1986, between APS, as lessee, and the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation, as lessor, as amended by Amendment No. 1 thereto, dated as of November 1, 1986; and

(ii) the Facility Lease, dated as of August 1, 1986, between APS, as lessee, and the Owner Trustee, as owner

trustee for Emerson Capital Corporation,
as lessor, as amended by Amendment No. 1
thereto, dated as of November 1, 1986.

(6) Participation Agreement means each
of:

(i) the Participation Agreement,
dated as of August 1, 1986, among the
Equity Participant designated therein,
the Company, Bank of America National
Trust and Savings Association, for itself
and as Agent for the banks named therein,
FNB, in its individual capacity and as
Owner Trustee for Security Pacific
Capital Leasing Corporation, Chemical
Bank, in its individual capacity and as
Indenture Trustee, and APS, as amended by
Amendment No. 1 thereto, dated as of
November 1, 1986; and

(ii) the Participation Agreement,
dated as of August 1, 1986, among the
Equity Participant designated therein,
the Company, Bank of America National
Trust and Savings Association, for itself
and as Agent for the banks named therein,
FNB, in its individual capacity and as
Owner Trustee for Emerson Capital
Corporation, Chemical Bank, in its indi-
vidual capacity and as Indenture Trustee,
and APS, as amended by Amendment No. 1
thereto, dated as of November 1, 1986.

SECURITY PACIFIC CAPITAL LEASING CORPORATION

November 19, 1986

CHEMICAL BANK

not in its individual
capacity, but solely as Collateral
Trust Trustee.

55 Water Street

New York, New York 10041

Attention: Corporate Trustee Administration

ARIZONA PUBLIC SERVICE COMPANY

PALO VERDE NUCLEAR GENERATING STATION UNIT 2 LEASE

Dear Sirs:

Reference is made to the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among the parties whose signatures appear at the foot hereof. All capitalized terms used herein without definition shall have the meanings set forth in Appendix A to the Participation Agreement.

1. Representations, Warranties and Agreements. Security Pacific Capital Leasing Corporation (the "Equity Participant"), Bank of America National Trust and Savings Association, for itself and as Agent, PVNGS Funding Corp., Inc., The First National Bank of Boston, as Owner Trustee, Chemical Bank, as Indenture Trustee and APS hereby confirm for your benefit that their respective representations and warranties (in the capacity given therein) and, in the case of APS, agreements, contained in Sections 6, 7, 8, 9, 10, 13 and 14 of the Participation Agreement and, in the case of the Equity Participant, the agreements contained in

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Section 14(a) of the Participation Agreement, are true and correct and hereby respectively repeat such representations, warranties and, in the case of APS and the Equity Participant, agreements to the same extent as if such representations, warranties and agreements were set forth herein in full, whether or not the same are amended after the date hereof.

2. Survival of Representations, Warranties and Agreements. All representations, warranties and agreements contained herein shall survive the execution and delivery of this letter.

3. Successors and Assigns. All terms and provisions of this letter shall inure to your benefit and the benefit of your successors and assigns and each holder from time to time of each Bond.

4. Consequences of Breach. A breach of the representations, warranties and agreements contained herein will not entitle you or any holder of a Bond to exercise remedies or take other action under the Participation Agreement or any other Transaction Document but you may pursue all other rights you have at law or in equity in consequence of such a breach.

5. Governing Law. This letter shall in all respects be governed by, and construed in accordance with, the laws of the State of New York.

6. Execution. This Extension Letter may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall constitute but one and the same instrument. Although this Extension Letter is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Extension Letter shall be effective on the latest of such dates.

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By: W. J. R.
Senior Vice President

Date: November 19, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION
for itself and as Agent for
the Original Loan
Participants

By: _____
Assistant Vice President

By: _____
Title: _____

Date: November , 1986

6. Execution. This Extension Letter may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall constitute but one and the same instrument. Although this Extension Letter is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Extension Letter shall be effective on the latest of such dates.

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By: _____
Senior Vice President

Date: November , 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION
for itself and as Agent for
the Original Loan
Participants

By: *[Signature]*
Assistant Vice President

By: *[Signature]*
Title: Group Vice President

Date: November 19, 1986

PVNGS FUNDING CORP., INC.

By: [Signature]
Vice President

Date: November 19, 1986

THE FIRST NATIONAL BANK OF
BOSTON
in its individual capacity
and as Owner Trustee

By: [Signature]
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK,
as Indenture Trustee

By: [Signature]
Vice President

Date: November 19, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By: [Signature]
Vice President and Treasurer

Date: November 19, 1986

SECURED LEASE OBLIGATION BONDS, SERIES 1986
COMMITMENT AGREEMENT

November 19, 1986

PVNGS Funding Corp, Inc.
1209 Orange Street
Wilmington, Delaware 19801

\$273,000,000
Secured Lease Obligation Bonds, Series 1986

Gentlemen:


Reference is made to (i) the Underwriting Agreement dated November 6, 1986 (the Underwriting Agreement) among Arizona Public Service Company, an Arizona corporation (APS), PVNGS Funding Corp, Inc., a Delaware corporation (Funding Corp), and The First Boston Corporation, Kidder Peabody & Co. Incorporated and Salomon Brothers Inc, individually and as representatives of the other underwriters identified therein (collectively, the Underwriters), providing for the purchase by the Underwriters, severally, of \$273,000,000 aggregate principal amount of Funding Corp's Secured Lease Obligation Bonds, Series 1986 (the Bonds) and (ii) the Collateral Trust Indenture dated as of November 1, 1986 (the Indenture), as supplemented by the Series 1986 Bond Supplemental Indenture dated as of November 15, 1986 (the Series 1986 Bond Supplemental Indenture), each among APS, Funding Corp and Chemical Bank, as Trustee (the Trustee), pursuant to which the Bonds are to be issued.

1. If APS, in a timely manner, provides Funding Corp with information sufficient for Funding Corp to direct the adjustments described in Section 7.01 of the Indenture or Section 1.04(b) of the Series 1986 Bond Supplemental Indenture, as the case may be, Funding Corp shall deliver to the Trustee a Company Request pursuant to such Section 7.01 or Section 1.04(b).

2. This Commitment Agreement has been executed and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York.

ARIZONA PUBLIC SERVICE
COMPANY

By


Title: Vice President and Treasurer

Accepted and agreed:

PVNGS FUNDING CORP,
INC.

By


Vice President

TAX INDEMNIFICATION AGREEMENT

dated as of August 1, 1986

between

SECURITY PACIFIC CAPITAL LEASING CORPORATION
as Equity Participant

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

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TAX INDEMNIFICATION AGREEMENT

THIS TAX INDEMNIFICATION AGREEMENT, dated as of August 1, 1986, is between SECURITY PACIFIC CAPITAL LEASING CORPORATION, a Delaware corporation (the "Equity Participant") and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Lessee"). Capitalized terms not otherwise defined herein shall have the meaning set forth in Appendix A to the Participation Agreement, dated as of August 1, 1986, among Security Pacific Capital Leasing Corporation, Bank of America, National Trust and Savings Association, PVNGS Funding Corp., Inc., The First National Bank of Boston, Chemical Bank and Arizona Public Service Company (the "Participation Agreement").

W I T N E S S E T H:

To induce the Equity Participant to execute the Participation Agreement, to make its investment as contemplated therein, to cause the Owner Trustee to purchase the Undivided Interest and the Real Property Interest and thereby to become entitled to the income tax attributes associated with ownership of the Undivided Interest and each element and component thereof and the Real Property Interest, and to induce the Equity Participant to enter into the Trust Agreement and to cause the Owner Trustee to lease the Undivided Interest and the Real Property Interest to the Lessee, and in full consideration of the foregoing, the Lessee irrevocably agrees, upon and in conformity with the terms hereof, to pay to the Equity Participant the indemnities as hereinafter set forth:

SECTION 1. Tax Assumptions and Tax Representations.

(a) Tax Assumptions. The Facility Lease has been entered into, and the Equity Participant's Net Economic Return has been computed, on the basis, inter alia, of the following tax assumptions (it being understood that nothing in this Section 1(a) is intended as a representation or warranty of the Lessee, except as expressly set forth in Section 1(b)):

(1) The Facility Lease will be treated as a true lease; the Owner Trustee will be treated as the purchaser, owner and lessor of the Undivided Interest;

and the Lessee will be treated as the lessee of the Undivided Interest.

(2) The Trust will be treated as a grantor trust which is subject to Subpart E, Part I, Subchapter J, Chapter 1 of Subtitle A (sections 671 through 679 inclusive) of the Code and the Regulations thereunder; the Equity Participant will be treated as the owner of the entire Trust; and the Equity Participant will be entitled to take into account, in computing the consolidated federal income tax liability of the affiliated group of corporations of which the Equity Participant is a member (the "Group") each item of income, gain, loss, deduction and credit of the Trust.

(3) For purposes of claiming the investment tax credit, the Equity Participant and the Owner Trustee will elect to treat the Lessee as having acquired the Undivided Interest pursuant to section 48(d) of the Code.

(4) For purposes of computing cost recovery deductions under the Accelerated Cost Recovery System provided in section 168 of the Code ("ACRS") with respect to the Undivided Interest, the Owner Trustee's basis for federal income tax purposes (determined without regard to increases in basis attributable to expenditures made by or on behalf of the Owner Trustee or the Equity Participant and not included in the Purchase Price) (the "Owner Trustee's Basis") will be at least equal to the portion of the Purchase Price allocated to the Undivided Interest in Schedule 3 to the Participation Agreement.

(5) Cost recovery deductions under ACRS will be allowed with respect to the Undivided Interest pursuant to sections 167(a), 168(a) and 168(b)(1) of the Code; the Equity Participant's taxable year in which the Closing Date occurs will be a full taxable year; and, provided that no election is made by the Equity Participant under section 168(b)(3) of the Code, the Equity Participant will be entitled to take such deductions into account in computing the consolidated federal income tax liability of the Group, in the taxable year of the Equity Participant which includes the Closing Date and each of its nine succeeding taxable years, in an amount determined by applying the "Applicable Percentage" for each such taxable year to the Owner Trustee's Basis in the Undivided Interest in accordance with the following table:

Taxable Year Ending
December 31

Applicable Percentage

1986	8%
1987	14%
1988	12%
1989	10%
1990	10%
1991	10%
1992	9%
1993	9%
1994	9%
1995	9%

(the deductions described in this paragraph (5) being hereinafter referred to as the "ACRS Deductions").

(6) The indebtedness evidenced by the Notes will constitute a loan made to the Owner Trustee; all amounts payable thereon as interest or premium will be deductible by the Equity Participant, when paid or accrued, pursuant to section 163 of the Code and the Regulations thereunder, in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income (the "Interest Deductions"); and the Equity Participant will be entitled to take the Interest Deductions into account in computing the consolidated federal income tax liability of the Group.

(7) The Equity Participant will be allowed current deductions for amortization of an amount equal to the Transaction Expenses computed on a straight-line basis over the Basic Lease Term (the "Amortization Deductions"); and the Equity Participant will be entitled to take the Amortization Deductions into account in computing the consolidated federal income tax liability of the Group.

(8) The Equity Participant will have at all relevant times sufficient federal taxable income against which to apply the ACRS Deductions, the Interest Deductions and the Amortization Deductions.

(9) The Notes will bear interest pursuant to their terms at the rates applicable from time to time; the principal amount of the Notes will constitute no more

than 80 percent of the Purchase Price; and the Notes will be amortized by certain payments of principal pursuant to the terms thereof.

(10) Basic Rent will be paid on December 30, 1986 and the Basic Rent Payment Dates. Basic Rent will be payable in semi-annual installments during the Basic Lease Term and each Renewal Term as set forth in the Facility Lease.

(11) Neither the Owner Trustee nor the Equity Participant (i) will at any time prior to the end of the Lease Term be required to include any amount in gross income for federal income tax purposes in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such items of property, other than any such payments required to be made on an After-Tax Basis pursuant to the Transaction Documents and (ii) will at any time be required to include any other amount in gross income for federal income tax purposes with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than (a) payments of Basic Rent, in the amounts and no earlier than at the times such payments are accrued in accordance with the terms of the Facility Lease, which payments of Basic Rent shall be accrued ratably over the six-month period (or portion thereof in the case of Basic Rent payable on December 30, 1986) ending June 30, in the case of each payment of Basic Rent due June 30, and ending December 31, in the case of each payment of Basic Rent due December 30, (b) payments of Casualty Value, Special Casualty Value and Extraordinary Casualty Value at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income, (c) amounts paid to the Equity Participant which are specifically identified as interest, (d) any amount paid to the Equity Participant with respect to which the Equity Participant is entitled to a contemporaneous and fully offsetting deduction, (e) any payments required to be made on an After-Tax Basis pursuant to the Transaction Documents, at the time such payments are made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income, (f) payments pursuant to the exercise of Lessee's options to purchase the Undivided Interest as described in the

Facility Lease at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income and (g) payments pursuant to the sale or other disposition of the Undivided Interest, other than as described in clause (f), at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income.

(12) The Equity Participant's combined marginal federal, state and local rate of income tax is 50.725%, without giving effect to any credits against tax and such combined marginal rate will be applicable to each item of income and deduction contemplated by this Section 1(a).

(13) The Equity Participant's cash investment in the Undivided Interest will be an amount equal to no less than 20% of the Purchase Price.

(14) The Closing Date will be August 18, 1986.

(15) For federal income tax purposes, the taxable year of the Equity Participant is the calendar year, and the Equity Participant will report all items of income, gain, loss or deduction relating to the transactions contemplated by the Transaction Documents using the accrual method of tax accounting except as otherwise contemplated by Section 1(a)(11) hereof in respect of Basic Rent.

(16) The Owner Trustee and the Equity Participant will be entitled to treat each item of income, gain, loss, deduction and credit with respect to the transactions contemplated by the Transaction Documents and the Financing Documents as derived from or allocable to sources within the United States.

(17) The Equity Participant will not be subject to the imposition of any surtax, "clawback tax", "user fee" or similar imposition, or to any at-risk limitation or restriction on the utilization of passive losses by reason of its participation in the transactions contemplated by the Transaction Documents and the Financing Documents, nor otherwise suffer an adverse effect on its anticipated Net Economic Return by reason of a Change in Tax Law.

(b) Tax Representations. The Lessee represents and warrants to and covenants with the Equity Participant that:

(1) On the Closing Date and throughout the Lease Term, the Undivided Interest and each item of property constituting the Undivided Interest will be "recovery property" and "10-year property" within the meaning of sections 168(c)(1) and 168(c)(2)(C) of the Code as in effect on the Closing Date.

(2) Unit 2, the Lessee's undivided interest in Unit 2 and each item of property constituting the Undivided Interest will have been "placed in service" for federal income tax purposes on or before the Closing Date.

(3) No item of property constituting the Undivided Interest and no portion of the Purchase Price will be subject to the provisions of section 168(f)(12) of the Code. No item of property constituting the Undivided Interest and no portion of the Purchase Price will be subject to the provisions of section 168(f)(10) of the Code.

(4) The Lessee has provided to the Ebasco Business Consulting Company all factual information in its possession which is relevant to the conclusions of Ebasco Business Consulting Company and such information is accurate and complete on the Closing Date. The Lessee has no reason to believe that the conclusions of Ebasco Business Consulting Company are inaccurate.

(5) Assuming that the Owner Trustee is the owner of the Undivided Interest for federal income tax purposes, the Equity Participant will be entitled to the ACRS Deductions, the Interest Deductions and the Amortization Deductions.

(6) Neither the Owner Trustee nor the Equity Participant (i) will at any time prior to the end of the Lease Term be required to include any amount in gross income for Federal income tax purposes in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such items of property, other than any such payments required to be made on an After-Tax Basis pursuant to the Transaction Documents and (ii) will at any time be required to include any other amount in

gross income for federal income tax purposes with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts described in Sections 1(a)(11)(ii)(a) through (g) hereof at the respective times referred to therein.

(7) The Owner Trustee and the Equity Participant will be entitled to treat each item of income, gain, loss and deduction with respect to the transactions contemplated by the Transaction Documents or the Financing Documents as derived from or allocable to sources within the United States within the meaning of section 861 of the Code and the Regulations promulgated thereunder.

(8) At all times prior to the Closing, the Undivided Interest will have been owned by the Lessee.

(9) The Equity Participant will not lose any of the tax benefits expected to be available to it with respect to the transactions contemplated by the Transaction Documents by reason of the application of section 168(e) of the Code to the transactions contemplated by the Transaction Documents.

(10) Throughout the Lease Term the Undivided Interest will not constitute "tax-exempt use property" within the meaning of section 168(j) of the Code and the provisions of section 168(j) of the Code as in effect on the Closing Date will not apply to the transactions contemplated by the Transaction Documents.

(11) No part of the Undivided Interest will be used predominantly outside the United States within the meaning of section 168(f)(2) of the Code.

(12) On the Closing Date, no improvements, modifications or additions to Unit 2 or the Undivided Interest will be required to render Unit 2 or the Undivided Interest complete for its intended use by the Lessee.

(13) All of the cost of the Undivided Interest or the Real Property Interest paid for or incurred by the Lessee or any Affiliate thereof will in each case have been reimbursed by the Owner Trustee through payment of the Purchase Price and the Real Estate Investment, respectively.

(14) On the Closing Date, the fair market value of the Undivided Interest will be the amount set forth as the Purchase Price in Schedule 3 to the Participation Agreement and the fair market value of the Real Property Interest will be the amount set forth as the Real Estate Investment in Schedule 3 to the Participation Agreement; and, assuming that the Owner Trustee is the owner of the Undivided Interest for federal income tax purposes, the Owner Trustee's Basis in the Undivided Interest and the Real Property Interest will in each case be at least equal to the Purchase Price and the Real Estate Investment, respectively.

(15) (i) It is reasonable to expect (x) that the Undivided Interest will be useful to and useable by a Person other than the Lessee or any Person related (within the meaning of section 318 of the Code) to the Lessee at the end of the Basic Lease Term and any Fixed Rate Renewal Term and capable of lease or transfer to such a Person at that time, and (y) that it will be commercially feasible for the Owner Trustee or the Equity Participant to enter into such a lease or transfer at such time in a transaction pursuant to which the Equity Participant would realize, with respect to the Undivided Interest, the residual value set forth in the report of Ebasco Business Consulting Company apart from any amounts that such a Person would be required to expend pursuant to the Assignment and Assumption or otherwise in connection with the acquisition or use of the Undivided Interest and apart from any amounts that such a Person would be required to expend in connection with the acquisition or use of the Real Property Interest and (ii) the Undivided Interest does not constitute, and will not constitute during the Lease Term, "limited use property" within the meaning of Revenue Procedure 76-30; provided, however, that this representation is not a representation that any residual value will in fact exist at the end of the Basic Lease Term and any Renewal Term.

(16) With respect to the Undivided Interest and the indebtedness evidenced by the Notes, neither the Lessee, any Affiliate nor any Person claiming by, through or under the Lessee or any Affiliate (other than the Owner Trustee, Equity Participant or any successor thereto) will at any time claim the ACRS Deductions, the Interest Deductions, the Amortization Deductions or any corresponding deduction under applicable state or local income tax law.

(17) The Equity Participant will not be required pursuant to section 467 of the Code to include in gross income any Rent at any time earlier than the time such payments are accrued in accordance with the terms of the Facility Lease.

(18) The Lessee does not legally or beneficially or constructively own (within the meaning of section 318 of the Code) any capital stock of the Loan Participants, Original Loan Participants, Funding Corp or any Holder of Bonds.

(19) Neither the Equity Participant nor the Owner Trustee will be treated as engaged in a partnership with any other Person as a result of the transactions contemplated by the Transaction Documents or the Financing Documents.

SECTION 2. Indemnification.

(a) Consistent Tax Returns. The Lessee agrees that neither it nor any Affiliate will at any time take any action, directly or indirectly, or file any returns or other documents inconsistent with the assumptions and representations set forth in Section 1 hereof, and that the Lessee and any such Affiliate will file such returns, maintain such records, take such actions and execute such documents, as reasonably requested by the Equity Participant from time to time, and as may be appropriate to facilitate the realization of such assumptions by the Equity Participant. The Lessee covenants and agrees to maintain, or cause to be maintained, such other records as shall be reasonably requested by the Equity Participant, in each case in order to verify the factual basis for the matters referred to in this Tax Indemnification Agreement. The Lessee shall make the records referred to in the preceding sentences (other than the Lessee's tax returns) available, or cause such records to be made available, for inspection by the Equity Participant or its authorized agents, during normal business hours at the Lessee's office at 411 North Central Avenue, Phoenix, Arizona 85072, Attention: Paul A. Williams, Vice President & Treasurer, upon request by, and five days' prior notice from, the Equity Participant. The Lessee shall, at its expense, upon request by the Equity Participant, provide to the Equity Participant a copy of such records which shall be certified to be a true copy by an affidavit attached thereto and executed by an officer of the Lessee. Notwithstanding the preceding sentence, the Equity

Participant or its authorized agents shall have the right to make copies and extracts of any such records at the Equity Participant's sole expense. The Lessee may, in accordance with its record retention practice and consistent with the requirements of the NRC, after written notice to the Equity Participant at least 30 days prior thereto, destroy such records as are specified in such notice other than those identified by the Equity Participant by written notice to the Lessee prior to such destruction.

(b) Indemnification--Loss of Tax Benefits. The Lessee shall indemnify the Equity Participant on an After-Tax Basis for

(1) any loss, disallowance, delay in obtaining, or recapture of the ACRS Deductions, the Interest Deductions or the Amortization Deductions; any loss, disallowance, delay in obtaining, or recapture of any credits for foreign taxes that otherwise would have been allowable to the Equity Participant; or any inclusion in gross income of any amount with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts set forth in Section 1(a)(11) hereof, at any time other than the times specified in Section 1(a)(11) hereof, in each case resulting in whole or in meaningful part from any one or more of the following events or circumstances:

(i) any representation or warranty of the Lessee in Section 1(b) hereof or elsewhere in this Tax Indemnification Agreement, the other Transaction Documents, the Financing Documents or any certificate or other document delivered by the Lessee in connection herewith or therewith, proving inaccurate at any time or the Lessee breaching any of its covenants in Section 1(b) hereof or any of its agreements, covenants, duties, undertakings or other obligations under this Tax Indemnification Agreement or the other Transaction Documents or the Financing Documents; or

(ii) any act or failure to act by the Lessee or by any Affiliate, transferee, sublessee, or assignee of the Lessee or by any user of the Undivided Interest, or by any person to whom the Lessee or any Affiliate thereof shall sell power or energy generated at PVNGS, or by any person having custody or possession of Unit 2 or the Undivided Interest or by any ANPP Participant or by any Affiliate of any

of the foregoing or by any subsequent transferee, sublessee or assignee or by any trustee, receiver, liquidator or debtor in possession of any of the foregoing, other than, in the case of the Lessee, the execution and delivery of one or more of the Transaction Documents or the Financing Documents and acts specifically required or expressly permitted to be performed by the Lessee under the Facility Lease or any Transaction Document or any Financing Document; provided, however, that (A) any act of the Lessee performed to satisfy a general covenant to comply with Applicable Laws or prudent utility practice or to cause the Undivided Interest to be operated and maintained or to carry out obligations under the ANPP Participation Agreement and related agreements, (B) any act that is permitted by implication or because it is not required or prohibited by such documents, (C) any act that implements a general requirement or right on the part of the Lessee in a manner that is not specifically required or expressly permitted under such documents, (D) the transfer, assignment, sublease or any other disposition (whether by merger or otherwise) by the Lessee, or any use by a Person other than the Lessee, of all or any part of its interest in the Undivided Interest and (E) the making of any Capital Improvement shall each be an act or failure to act for which the lessee is responsible under this paragraph (ii), or

(iii) the sale or other disposition of Unit 2, the Undivided Interest or any item of property constituting the Undivided Interest upon the exercise by the Equity Participant of its remedies under the Facility Lease upon the occurrence of an Event of Default thereunder, or

(iv) the bankruptcy, or other proceedings for the protection of debtors, of or involving the Lessee or any transferee, sublessee or assignee of the Lessee or any subsequent transferee, sublessee or assignee or any Affiliate of any of the foregoing, or any foreclosure on any property of any of the foregoing, or

(v) any damage to or destruction, loss of generating capacity, theft, nongovernmental taking or requisition or repair of or any addition, improvement, modification, alteration, replacement

or substitution of or to Unit 2 or the Undivided Interest or the Real Property Interest, or any part thereof, or any Event of Loss or Deemed Loss Event, or any event which, with the passage of time or the giving of notice or both, would constitute such an event, or

(vi) any governmental taking or requisition of title, use or otherwise of Unit 2, the Undivided Interest or the Real Property Interest or any part thereof if such taking or requisition does not immediately constitute an Event of Loss under the Facility Lease, or

(vii) any payment by any manufacturer or any other vendor or supplier or contractor or subcontractor with respect to any part of Unit 2 or the Undivided Interest, but in the event of any such payment made to the Equity Participant, any indemnity hereunder shall take into account any economic benefit realized by the Equity Participant from the receipt of such payment without double counting for any economic loss for which such payment provided compensation, or

(viii) any issuance, defeasance, refinancing, refunding, redemption, purchase, repurchase, cancellation, retirement, reamortization, reoptimization, substitution, releveraging, modification or remarketing of the Notes, or the Bonds, or any other debt securities issued or assumed pursuant to the Transaction Documents or the Financing Documents or any terms or provisions thereof or otherwise in connection with the financing, refinancing or any Supplemental Financing of Unit 2, any Capital Improvement or the Undivided Interest or the Real Property Interest or any part thereof or interest therein, including, without limitation, the purchase or deemed purchase by the Lessee, Funding Corp, the Loan Participants or the Original Loan Participants of any such Notes, Bonds or securities, or the existence of any of the Lessee's rights to effect any of the foregoing, or

(ix) the presence of Funding Corp, or any successor or assign thereof, in the transactions contemplated by the Transaction Documents and the Financing Documents, or

(x) the existence or operation of the ANPP Participation Agreement, the ANPP Project Agreements or any amendment to any of the foregoing (including without limitation the rights and remedies of the ANPP Participants) or any obligations of the Lessee or restriction of rights of the Owner Trustee or the Equity Participant or provisions of any of the Transaction Documents or the Financing Documents (including without limitation the provisions of the Assignment and Assumption) resulting from any of the foregoing, or

(xi) the existence, provisions or operation of the License or the License Amendment, or

(xii) the existence, provisions or operation of Title USA Company of Arizona Trust No. 530, or

(xiii) the existence or implementation of the provisions (w) set forth in Section 10(b)(3)(ix) of the Participation Agreement relating to the rights of the Lessee to purchase the Undivided Interest if it fails to renew the Letter of Credit, (x) set forth in Section 10(b)(3)(viii) of the Participation Agreement, (y) set forth in Section 5 of the Facility Lease and Sections 15(iii) and 16(a)(vii) of the Facility Lease and (z) providing for Deemed Loss Events, or

(xiv) without limiting the generality of the foregoing clause (xiii) of this Section 2(b)(1), the maintenance or creation of any decommissioning fund pursuant to Section 10(b)(3)(viii) of the Participation Agreement (the "Decommissioning Fund"); the investment or the failure to invest money held in the Decommissioning Fund; the earning of investment income, the failure to earn investment income or the realization of any gain or loss with respect to the investment of money held in the Decommissioning Fund; or any act or failure to act with respect to the Decommissioning Fund (whether or not such act or failure to act is permitted or required under the Transaction Documents or the Financing Documents) of the trustee of either thereof, the Lessee, any Affiliate of the Lessee or any other Person,

(2) any inclusion in the Equity Participant's gross income, for federal income tax purposes, of any amount in respect of any replacement or substitution of, or any alteration to or modification in any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such item of property or pursuant to the Transaction Documents or Financing Documents (whether or not permitted or required under the Transaction Documents or Financing Documents) or any inclusion prior to the end of the Lease Term in the Equity Participant's gross income, for federal income tax purposes, of any amount in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or the Real Property Interest or any expenditure made or property furnished by the Lessee in respect of such item of property or pursuant to the Transaction Documents or Financing Documents (whether or not permitted or required under the Transaction Documents or Financing Documents) and

(3) any loss, disallowance, delay in obtaining or recapture of the ACRS Deductions, the Interest Deductions or the Amortization Deductions; any loss, disallowance, delay in obtaining or recapture of any credits for foreign taxes that otherwise would have been allowed to the Equity Participant; any inclusion in gross income of any amount with respect to any transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts set forth in Section 1(a)(11) hereof, at any time other than the times specified in Section 1(a)(11) hereof; or the imposition of any restriction on the use of any benefit contemplated by the assumptions set forth in Section 1(a) hereof or the imposition of any surtax or similar imposition or suffering described in Section 1(a)(17) hereof, in each case resulting in whole or in part from a Change in Tax Law

(any such loss, disallowance, delay in obtaining, recapture, imposition or inclusion in respect of either subsection (1) or (2) above or this subsection (3) being hereinafter referred to as a "Tax Loss").

(c) Indemnity Payment - After-Tax Basis.

(1) In the event of a Tax Loss, the Equity Participant, unless pursuant to Section 5 hereof the Equity Participant is not entitled to payment with respect to such

Tax Loss, shall give notice in writing to the Lessee of such Tax Loss accompanied by a written statement describing in reasonable detail such Tax Loss and the computation of the amount payable, and the Lessee shall pay to the Equity Participant on an After-Tax Basis in a lump sum on the Effective Date an amount (the "Indemnity Payment") which, after giving effect to such Tax Loss and any interest, penalties or additions to tax payable as a result of such Tax Loss, will be sufficient to provide the Equity Participant the same Net Economic Return (after taking into account any future loss or losses of federal income tax benefits, and any past, present or future federal income tax benefits expected to be available to the Equity Participant, in each case, in the reasonable determination of the Equity Participant, generated as a result of the Tax Loss with respect to which the Indemnity Payment is being determined, the circumstances giving rise thereto or the determination thereof) that the Equity Participant would have realized if it had not suffered such Tax Loss.

(2) Notwithstanding the foregoing, if (a) the Lessee shall have provided a letter of credit or other financial support to the Equity Participant in amount, form and substance satisfactory to the Equity Participant in its sole discretion and (b) no Event of Default shall have occurred and be continuing, the Lessee may elect to pay an Indemnity Payment in equal semiannual payments to the Equity Participant (which payments do not constitute Basic Rent) on each Basic Rent Payment Date during the Basic Lease Term, commencing with the Effective Date; provided, however, that the amount of such payments shall in all events be calculated in a manner which preserves the Equity Participant's Net Economic Return. The Lessee shall give notice in writing to the Equity Participant of its election as to the mode of payment of any Indemnity Payment no later than 10 Business Days prior to the Effective Date of such Indemnity Payment.

SECTION 3. Determination of Payments.

Whenever it may be necessary for purposes of this Tax Indemnification Agreement to determine (a) the amount of any Tax Loss suffered by the Equity Participant or (b) the amount of any past, present or future tax benefits reasonably expected to be available to it, such determination shall be made on the assumptions that (a) the income taxes of the Equity Participant are payable at the combined marginal federal, state and local tax rate set forth in Section 1(a)(12) hereof, as such assumed combined marginal rate may

be modified to reflect a different marginal federal tax rate as a result of an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease in connection with a Change in Tax Law (the "Effective Rate"), (b) in computing its federal income tax liability, the Equity Participant could have fully utilized the tax benefits that are the subject of such Tax Loss against taxes payable at the Effective Rate and (c) the Equity Participant can fully utilize any tax benefits required to be taken into account under Section 2(c)(1) hereof resulting from a Tax Loss against federal income taxes payable at the Effective Rate.

The determination of the amount payable to or by the Equity Participant under this Tax Indemnification Agreement shall be made in the first instance by the Equity Participant, who shall furnish the Lessee with a notice setting forth in reasonable detail the computations and methods used in computing such amount; and, if requested by the Lessee, such determination shall be verified in writing by a firm of nationally recognized independent public accountants selected by the Equity Participant and acceptable to the Lessee, provided that, if a firm of nationally recognized independent public accountants regularly audits the books of the Equity Participant, then such firm shall be deemed to be acceptable to the Lessee. The costs of such verification shall be borne by the Lessee unless, as a result thereof, the amount payable to the Equity Participant is less than the amount originally determined by the Equity Participant by 10 percent or more of such amount in which case such costs shall be paid by the Equity Participant. Any statements furnished to the Lessee pursuant to Section 3 hereof shall (a) be signed by a Responsible Officer of the Equity Participant, (b) state in reasonable detail the basis upon which such amount or adjustment has been determined and (c) certify that such amount or adjustment has been determined pursuant to and in compliance with this Tax Indemnification Agreement. The Lessee agrees that it will not have the right to inspect the tax returns, books, records or any other documents of the Equity Participant or any Affiliate thereof in order to verify the basis or the accuracy of the calculations so made or of the amounts set forth in any such statement and that the determinations made by the independent accountants in accordance with this Section 3 shall be conclusive and binding.

SECTION 4. Effective Date.

An Indemnity Payment shall be due and payable 20 days after the date of the Equity Participant's notice to the

Lessee pursuant to Section 2(c)(1) hereof, or in the case of an Indemnity Payment relating to a Tax Loss which results from a proposed adjustment of the IRS that was contested pursuant to Section 6 hereof, 20 days after a Final Determination (as defined in Section 6(e) hereof) with respect to such Tax Loss; provided, however, that if the Lessee elects to pay an Indemnity Payment by way of semiannual payments pursuant to Section 2(c)(2) hereof, such payments shall commence on the first Basic Rent Payment Date occurring after the date of the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or, in the case of an Indemnity Payment relating to a Tax Loss that results from a proposed adjustment of the IRS that is contested pursuant to Section 6 hereof, on the first Basic Rent Payment Date occurring 20 days or more after a Final Determination with respect to such Tax Loss (the "Effective Date"). Notwithstanding anything to the contrary contained in the foregoing portion of this Section 4, and subject to Section 6 hereof as described below in this sentence, in the event of the expiration of the Basic Lease Term or the earlier termination of the Lease prior to the Effective Date of any Indemnity Payment, the Lessee shall pay to the Equity Participant on demand in a lump sum any such Indemnity Payment to the extent then unpaid; provided, however, that in no event shall the Lessee be required to pay all or any portion of any such Indemnity Payment prior to (x) the date 20 days after the date of the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or (y) if any such Indemnity Payment relates to a Tax Loss that is contested pursuant to Section 6 hereof, the date 20 days after the date of a Final Determination with respect to such Tax Loss. If pursuant to Section 3 hereof the Lessee requests verification of the computation of an Indemnity Payment, and such verification is not complete on the Effective Date then (i) the Lessee shall pay to the Equity Participant on the Effective Date the amount of the Indemnity Payment set forth in the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or the amount of the semiannual payment pursuant to Section 2(c)(2) hereof then due and payable, as the case may be, (ii) if the verification results in an upward adjustment to such Indemnity Payment or semiannual payment, the Lessee shall pay to the Equity Participant within 5 days after such verification is complete the amount of such upward adjustment with interest at the Prime Rate from the Effective Date to the date of payment and (iii) if the verification results in a downward adjustment to such Indemnity Payment or semiannual payment, the Equity Participant shall reimburse to the Lessee within 5 days after such verification is complete the amount

of such downward adjustment with interest at the Prime Rate from the Effective Date to the date of payment.

SECTION 5. Excluded Events.

The Equity Participant shall be responsible for, and shall not be entitled to any payment in respect of any Tax Loss occurring primarily as a direct result of one or more of the following events:

(a) a failure of the Equity Participant to claim in a proper or timely manner the ACRS Deductions, the Interest Deductions or the Amortization Deductions for the appropriate years (any disclosure or failure to make a disclosure pursuant to section 6661 of the Code shall not cause a claim to be considered improper), unless (i) the claiming of any such deductions would be inconsistent with any prior audit adjustment by the IRS with respect to which the Lessee is required to indemnify the Equity Participant under this Tax Indemnification Agreement (except to the extent such prior audit adjustment is being contested in accordance with the provisions of Section 6 hereof), (ii) the Equity Participant shall have furnished the Lessee, at the Lessee's sole cost and expense, with an opinion of independent tax counsel (selected by the Equity Participant and reasonably satisfactory to the Lessee) to the effect that as a result of a Change in Tax Law, Event of Loss, Deemed Loss Event, Termination Event, or an act, omission or misrepresentation of the Lessee such claim would not be proper pursuant to the standards of ABA Formal Opinion 85-352 or (iii) such failure to claim any such deductions for the appropriate year is caused by a failure of the Lessee to take any action or provide the Equity Participant with any information or document that the Lessee is required to take or provide pursuant to the Transaction Documents or the Financing Documents;

(b) the failure of the Equity Participant to have sufficient federal taxable income to benefit from the ACRS Deductions, the Interest Deductions, or the Amortization Deductions; provided, however, that such failure shall not be taken into account in determining the amount of any indemnity otherwise payable hereunder;

(c) any voluntary sale by the Equity Participant or any involuntary sale or other disposition resulting from the bankruptcy of, the foreclosure against, or any

similar proceeding against, the Equity Participant or the Owner Trustee, of the Undivided Interest, the Trust Estate, or any beneficial interest therein, unless such bankruptcy, foreclosure or similar proceeding relates to the transactions contemplated by the Transaction Documents, or an Event of Default shall have occurred and be continuing;

(d) (i) any Event of Loss or Deemed Loss Event whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, Casualty Value or Special Casualty Value for all of the Undivided Interest, (ii) any termination of the Facility Lease, whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, Casualty Value or Extraordinary Casualty Value for all of the Undivided Interest, or (iii) the exercise of the Cure Option, whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, the greater of Fair Market Sales Value and Casualty Value for all of the Undivided Interest except to the extent the payment made with respect to such Event of Loss, Deemed Loss Event, termination or exercise did not properly reflect the time of the occurrence of such Event of Loss, Deemed Loss Event, termination or exercise;

(e) any amendment, modification, deletion, addition or change in or to the provisions of the Code which shall occur after the Closing Date; provided, however, that the foregoing exclusion shall not apply (i) to a Change in Tax Law unless there has been a rent adjustment pursuant to Section 3(d) of the Facility Lease for such Change in Tax Law and (ii) to any Tax Loss which results from the inaccuracy of any representation made after the Closing Date by the Lessee in connection with a Change in Tax Law, and provided, further, that the foregoing exclusion shall not apply if such Tax Loss is a result in whole or in meaningful part of any act or failure to act (other than any act specifically required or expressly permitted to be performed by the Lessee under the Facility Lease or any Transaction Document, subject to the proviso in Section 2(b)(1)(ii) hereof), after the date of enactment of such amendment, modification, deletion, addition or change, by any person referred to in Section 2(b)(1)(ii) hereof;

(f) the application of Section 168(f)(5) of the Code to the Equity Participant solely because any taxable year of the Equity Participant is not a full taxable year;

(g) the inability of the Equity Participant to claim the ACRS Deductions, the Interest Deductions or the Amortization Deductions due to the Equity Participant or any Affiliate thereof or any predecessor of any thereof, being or becoming an entity subject to the provisions set forth in section 168(e)(3), 168(f)(11), 168(j), 465, 501, 593, 851, 856, 871, 881, 1361, 1381, 1391 or other similar provision of the Code relating to the status of the Equity Participant, unless such inability results from (i) in the case of section 168(e)(3) of the Code, the transactions contemplated by the Transaction Documents or (ii) a Change in Tax Law;

(h) the failure of the transaction to qualify as a "true lease" for federal income tax purposes, resulting in the Equity Participant not being treated as the owner of the Undivided Interest for federal income tax purposes, unless such failure is the result in whole or in meaningful part of an event or circumstance set forth in Section 2(b) hereof;

(i) the failure of the Equity Participant to fulfill its material obligations to contest a proposed adjustment or adverse determination as provided in Section 6 hereof; and

(j) the failure of the Owner Trust to be taxed as a conduit entity unless such failure arises as the result of an event or circumstance set forth in Section 2(b).

SECTION 6. Contests.

For purposes of defining the amount, if any, of Lessee's indemnity obligations hereunder:

(a) If the IRS proposes in writing an adjustment to the federal income tax liability of the Equity Participant, which adjustment, if sustained, would result in a Tax Loss, the Equity Participant shall notify the Lessee promptly of such adjustment and of all action taken or proposed to be taken by the IRS, and the Equity Participant shall for at least 30 days after giving such notice forbear, if such forbearance is permitted by law, payment of any tax (including interest, penalties and additions to tax thereon) asserted to be payable as a result of such proposed adjustment.

(b) If the Lessee requests within 30 days after the Equity Participant's notice pursuant to paragraph (a) of this Section 6 that the proposed adjustment be contested, the Equity Participant shall contest the proposed adjustment in good faith at the trial court level upon receipt of an opinion, furnished at the Lessee's sole cost and expense and setting forth the facts and legal analysis on which it is based, of independent tax counsel of nationally recognized standing selected by the Equity Participant and reasonably satisfactory to the Lessee to the effect that there exists a basis in law and fact under the standard imposed by ABA Formal Opinion 85-352 for such contest and at each appellate level upon receipt of an opinion furnished at the Lessee's sole cost and expense and setting forth the facts and legal analysis on which it is based, of independent tax counsel of nationally recognized standing selected by the Equity Participant and reasonably satisfactory to the Lessee to the effect that it is more likely than not that an appellate court will reverse or substantially modify the lower court decision, provided that (i) the Equity Participant shall be entitled to pursue or forego any administrative proceedings (except that the Equity Participant shall be required to pursue all reasonable administrative proceedings in the event judicial proceedings shall be unavailable by reason of a Tax Loss decreasing a net operating loss carryover, and in all events, the Equity Participant shall be required to pursue such administrative proceedings as shall be necessary to preserve available judicial proceedings), shall be required to contest any proposed adjustment beyond the level of administrative proceedings only if timely requested by the Lessee and shall not be required to pursue any appeal to the United States Supreme Court, (ii) the Equity Participant shall determine the court of competent jurisdiction in which to contest the proposed adjustment either before or after payment of the tax asserted to be payable as a result thereof, and (iii) the Equity Participant shall keep the Lessee informed as to the progress of any litigation and, if requested by the Lessee, shall consult with the Lessee's counsel (provided that the conduct of all administrative proceedings and litigation shall nevertheless remain within the sole discretion of the Equity Participant and its tax counsel exercised in good faith and provided, further, that the Equity Participant shall not discriminate (except with respect to selecting the forum in which to contest such proposed adjustment) against any such proposed adjustment as compared to other proposed adjustments made by the IRS

involving the potential tax liability of the Equity Participant). The Equity Participant shall not be required to take any action pursuant to this paragraph (b) of this Section 6 unless: (i) the amount of the Indemnity Payment arising from all proposed adjustments with respect to a taxable year, plus all indemnities that would arise by reason of the fact that the subject matter of any such adjustments is of a continuing nature, shall be in excess of \$500,000; (ii) the Lessee shall have agreed to indemnify the Equity Participant in a manner satisfactory to the Equity Participant for any expense which the Equity Participant may incur as a result of contesting such proposed adjustment; (iii) the Lessee shall have agreed to pay the Equity Participant on demand all reasonable costs and expenses that the Owner Participant may incur in connection with contesting such proposed adjustment (including, without limitation, reasonable legal and accounting fees, disbursements, penalties, interest and additions to tax); (iv) the Lessee shall have acknowledged its liability to the Equity Participant for an Indemnity Payment pursuant to this Tax Indemnification Agreement as a result of such proposed adjustment if and to the extent the Equity Participant shall not prevail in the contest of such proposed adjustment; (v) no Event of Default shall have occurred and be continuing; and (vi) the Equity Participant shall have determined that the action to be taken will not result in any danger of sale, forfeiture or loss of, or the creation of any Lien (except for Liens permitted under the Transaction Documents and except if the Lessee shall have adequately bonded such Lien or otherwise made provision to protect the interests of the Equity Participant in a manner satisfactory to the Equity Participant) on the Undivided Interest, the Real Property Interest, Unit 2 or any part thereof or interest therein. The Equity Participant shall also not be required to contest any proposed adjustment if the subject matter thereof shall be of a continuing nature and shall have previously been decided pursuant to the contest provisions of this Section 6, unless, subject to the other provisions of this Section 6, there shall have been a change in the law (including, without limitation, amendments to statutes or regulations, administrative rulings and court decisions) after such previous contest shall have been so decided, and the Equity Participant shall have received an opinion, setting forth the facts and legal analysis on which it is based, of independent tax counsel selected as provided in this Section 6(b) and furnished at the Lessee's sole expense to the effect that

the prior authorities are no longer determinative of the issue and that under such new law there exists a basis in law and fact under the standard imposed by ABA Formal Opinion 85-352 to contest such proposed adjustment.

(c) If the Equity Participant shall elect to contest a proposed adjustment by paying the tax claimed (including such other amounts payable as interest, penalties, or additions to tax) and seeking a refund, and if the proposed adjustment would be a Tax Loss with respect to which the Lessee could be required to indemnify the Equity Participant under this Tax Indemnification Agreement, then the Lessee shall advance to the Equity Participant on an interest-free basis and with no additional net after-tax cost to the Equity Participant the aggregate amount of such taxes, interest, penalties and additions to tax which the Equity Participant shall have elected to pay. If the Equity Participant subsequently receives a refund (or if the Equity Participant would have received a refund but for the fact that funds advanced by the Lessee were applied in payment of a tax liability of the Equity Participant for which the Lessee is not required to make an Indemnity Payment pursuant to this Tax Indemnification Agreement) of such taxes, interest, penalties or additions to tax, the Equity Participant shall promptly pay to the Lessee the amount received (or which would have been received) as a refund of such taxes, interest, penalties or additions to tax plus the amount of any interest received (or which would have been received) by the Equity Participant from the taxing authority with respect to such refunded taxes, interest, penalties or additions to tax; provided, however, that the Equity Participant shall not be obligated to refund to the Lessee any amount applied to a tax liability of the Equity Participant (or interest with respect thereto) if the IRS would have been foreclosed from asserting such tax liability but for the contest of such proposed adjustment; and provided, further, that the Equity Participant may offset the amount of such refunded taxes, interest, penalties or additions to tax and interest received or avoided against any amount due and owing by the Lessee to the Owner Participant pursuant to this Tax Indemnification Agreement.

(d) Notwithstanding anything to the contrary contained in this Section 6, the Equity Participant may at any time decline to take any further action with respect to a proposed adjustment or may settle any

contest without the consent of the Lessee; provided, however, that if the Lessee has properly requested the Equity Participant to contest such proposed adjustment pursuant to paragraph (b) of this Section 6 and shall have duly complied with all of the terms of this Section 6, the Equity Participant shall thereby waive its right to any Indemnity Payment by the Lessee that would otherwise be payable by the Lessee pursuant to this Tax Indemnification Agreement in respect of such adjustment, including any indemnities arising solely from such adjustment in subsequent years or which would arise by reason of the fact that the subject matter of such adjustment is of a continuing nature, unless in either case the contest of the adjustment giving rise to such indemnities is not precluded by the Equity Participant so declining or settling. In such event, the Equity Participant shall, within 30 days of such notice, reimburse the Lessee for all amounts previously advanced by the Lessee to the Equity Participant pursuant to paragraph (c) of this Section 6 including any interest received by the Equity Participant or the payment of which is actually avoided by reason of payment of the tax claimed with funds advanced by the Lessee.

(e) If the Lessee shall have appropriately requested the Equity Participant to contest any proposed adjustment as above provided and shall have duly complied with all of the terms of this Section 6, the amount of the Lessee's liability for indemnification pursuant to this Tax Indemnification Agreement shall become fixed upon a Final Determination of the liability of the Equity Participant for the tax and any interest, penalties and additions to tax asserted to be payable as a result of such proposed adjustment. A "Final Determination" with respect to a Tax Loss shall mean (i) a decision, judgment, decree or other order by any court of competent jurisdiction, which decision, judgment, decree or other order has become final (i.e., when all allowable appeals have been exhausted by either party to the action to the extent required by this Section 6) or, in any case where judicial review shall at the time be unavailable by reason of the proposed adjustment involving a decrease in a net operating loss carryforward, a decision, judgment, decree or other order of an administrative official or agency of competent jurisdiction, which has become final (i.e., all administrative appeals have been exhausted by either party to the extent required by this Section 6), (ii) a closing agreement entered into under section 7121 of the Code or any other settlement agreement entered

into in connection with an administrative or judicial proceeding, or (iii) the expiration of the time for instituting a claim for refund, or if such a claim was filed, the expiration of the time for instituting suit with respect thereto. Notwithstanding anything in this Section 6 to the contrary, the Equity Participant shall not be required to make any payments to the Lessee under this Section 6 while there shall be an amount due and owing by the Lessee to the Equity Participant under any of the Transaction Documents, or if and for so long as an Event of Default shall have occurred and be continuing.

SECTION 7. Adjustments.

The tax assumptions and the Lessee's representations set forth in Sections 1(a) and 1(b) hereof shall be modified to the extent necessary and appropriate to reflect any adjustments to Basic Rent provided for in Section 3(d) or 3(e) of the Facility Lease or the payment of an Indemnity Payment so as to reflect any Change in Tax Law or any Tax Loss in the manner in which it was taken into account in computing such adjustment or Indemnity Payment.

SECTION 8. Affiliated Group.

For purposes of this Tax Indemnification Agreement, the term "Equity Participant" shall include any member of an affiliated group of corporations of which the Equity Participant is, or may become, a member if consolidated returns are or shall be filed for such affiliated group for federal income tax purposes.

SECTION 9. Duration.

The obligations and liabilities of the Equity Participant and the Lessee arising under this Tax Indemnification Agreement shall continue in full force and effect, notwithstanding the expiration or early termination of the Facility Lease, until all such obligations have been met and such liabilities have been paid in full, and shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

SECTION 10. Payments.

All payments to be made to the Equity Participant or the Lessee pursuant to this Tax Indemnification Agreement shall be made in immediately available funds to such bank and/or account in the continental United States for the account of the Equity Participant or the Lessee as from time to time the Equity Participant shall have directed the Lessee or the Lessee shall have directed the Equity Participant, as the case may be, in writing. If the date on which any payment to be made pursuant to this Tax Indemnification Agreement shall not be a Business Day, such payment shall be made on the next succeeding Business Day.

SECTION 11. Interest.

Interest at the Penalty Rate shall be payable on any amount not paid when due hereunder until such amount shall be paid.

SECTION 12. Notices.

All notices and other communications provided for herein shall be given to the Equity Participant or the Lessee, as the case may be, in the manner and to the appropriate address, and shall become effective, as provided in Section 17 of the Facility Lease.

SECTION 13. No Setoff.

Except in accordance with the express terms hereof, (a) no payment required to be made by the Lessee pursuant to this Tax Indemnification Agreement shall be subject to any right of setoff, counterclaim, defense, abatement, suspension, deferment or reduction, and (b) the Lessee shall have no right to terminate this Tax Indemnification Agreement, or to be released, relieved or discharged from any obligation or liability under this Tax Indemnification Agreement for any reason whatsoever except as expressly provided herein.

SECTION 14. Governing Law.

This Tax Indemnification Agreement shall be governed by and construed in accordance with the laws of the State of New York.

SECTION 15. Counterparts.

This Tax Indemnification Agreement may be executed in any number of counterparts, each of which so executed shall be deemed to be an original, and such counterparts together shall constitute and be one and the same instrument.

SECTION 16. Headings.

The headings of the sections of this Tax Indemnification Agreement have been inserted for convenience of reference only and shall in no way restrict or otherwise modify any of the terms or provisions hereof.

SECTION 17. Amendments, Supplements, etc.

Neither this Tax Indemnification Agreement nor any of the terms hereof may be amended, supplemented, waived or modified orally, but only by an instrument in writing signed by the party against which enforcement of such change is sought.

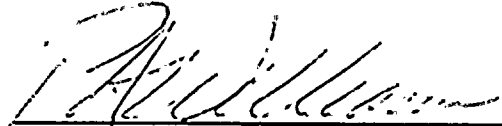
SECTION 18. No Duplication of Payment.

Nothing contained in the terms of this Tax Indemnification Agreement or any other Transaction Document shall be construed to require the Lessee to make any payment with respect to any Tax Loss more than once or to make any payments hereunder to the extent previously reflected in a rental adjustment pursuant to Section 3(d) of the Facility Lease, otherwise, the Lessee's obligations hereunder are absolute and unconditional and are payable independent of and from the Facility Lease, the Participation Agreement and any other circumstance whatsoever.

IN WITNESS WHEREOF, the Equity Participant and the Lessee have caused this Tax Indemnification Agreement to be duly executed by their respective officers thereunto duly authorized as of the date set forth below.

ARIZONA PUBLIC SERVICE COMPANY

By


Vice President

Dated: 8-18-86

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By _____

Dated:

IN WITNESS WHEREOF, the Equity Participant and the Lessee have caused this Tax Indemnification Agreement to be duly executed by their respective officers thereunto duly authorized as of the date set forth below.

ARIZONA PUBLIC SERVICE COMPANY

By _____
Vice President

Dated:

SECURITY PACIFIC CAPITAL
LEASING CORPORATION

By 727

Dated: 8-18-86

REIMBURSEMENT AGREEMENT

between

Arizona Public Service Company

and

Morgan Guaranty Trust Company of New York

dated as of

August 1, 1986

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REIMBURSEMENT AGREEMENT

REIMBURSEMENT AGREEMENT, dated as of August 1, 1986 between Arizona Public Service Company, an Arizona corporation (the "Company"), and MORGAN GUARANTY TRUST COMPANY OF NEW YORK (the "Bank").

WHEREAS, the Company has entered into a Participation Agreement dated as of August 1, 1986 among the Company, The First National Bank of Boston, for itself and as Owner Trustee (the "Owner Trustee"), Chemical Bank, for itself and as Indenture Trustee, Bank of America National Trust and Savings Association, for itself and as Agent for the Loan Participants, PVNGS Funding Corp, Inc. and Security Pacific Capital Leasing Corporation, as Equity Participant (the "Equity Participant") relating to the acquisition of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station through a trust for the benefit of the Equity Participant which interest will be leased to the Company pursuant to a lease dated as of August 1, 1986 between the Owner Trustee and the Company (the "Facility Lease"); and

WHEREAS, it is a condition precedent to the Owner Trustee's making available, on behalf of the Equity Participant, the Purchase Price of Unit 2 that the Bank issue to the Equity Participant an irrevocable letter of credit in the form of Exhibit A hereto (the "Letter of Credit"); and

WHEREAS, the Bank is willing to issue the Letter of Credit on the terms and subject to the conditions set forth in this Agreement;

NOW, THEREFORE, the Bank and the Company hereby agree as follows:

SECTION 1. (a) Definitions. Capitalized terms used herein and not otherwise defined herein shall have the respective meanings assigned thereto in Appendix A to the Facility Lease. The following terms, as used herein, have the following respective meanings:

"Aggregate Operating Lease Obligations" of any Person means all Operating Lease Obligations under operating leases which are entered into by such Person in substantially contemporaneous transactions.

"Agreement" means this Reimbursement Agreement, as the same may from time to time be amended, supplemented or modified.

"Business Day" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close.

"Code" means the United States Internal Revenue Code of 1954, as amended.

"Company Indenture" means the Mortgage and Deed of Trust dated as of July 1, 1946, as amended and supplemented at the date hereof, of Central Arizona Light and Power Company (now the Company) to Security-First National Bank of Los Angeles (now Security Pacific National Bank), as Trustee..

"Controlled Group" means all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Company, are treated as a single employer under Section 414(b) or 414(c) of the Code.

"Consolidated Subsidiary" means at any date any subsidiary or other entity the accounts of which would be consolidated with those of the Company in the Company's consolidated financial statements as of such date.

"Date of Early Termination" has the meaning set forth in the Letter of Credit.

"Date of Issuance" means the date on which the Letter of Credit is issued upon request of the Company pursuant to Section 3(a) hereof.

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

"Fixed Charge Ratio" has the meaning set forth in Section 7(i) hereof.

"Funded Indebtedness" means all Indebtedness which matures more than one year from the date of its creation or matures within one year from such date but is renewable or extendible, at the option of the Company, to a date more than one year from such date or arises under a revolving credit or similar agreement which obligates the lender or lenders to extend credit during a period of more than one year from such

date including, without limitation, all amounts of Funded Indebtedness required to be paid or prepaid within one year from the date of its creation.

"Guaranteed Indebtedness" of any Person means all Indebtedness referred to in clause (i), (ii) or (iii) of the definition of "Indebtedness" guaranteed directly or indirectly in any manner by such Person, or in effect guaranteed directly or indirectly by such Person through an agreement (i) to pay or purchase such Indebtedness or to advance or supply funds for the payment or purchase of such Indebtedness, or (ii) to purchase, sell or lease (as lessee or lessor) property, or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such Indebtedness or to assure the holder of such Indebtedness against loss, or (iii) to supply funds to or in any other manner invest in the debtor (including any agreement to pay for property or services irrespective of whether or not such property is received or such services are rendered), or (iv) otherwise to assure a creditor against loss.

"Imputed Rate" means, in respect of Indebtedness, the actual initial rate of interest to be paid by a Person with respect to such Indebtedness.

"Indebtedness" of any Person means (i) all indebtedness of such Person for borrowed money or for the deferred purchase price of property or services, (ii) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property acquired by such Person (even though the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property), (iii) all obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, recorded as capital leases in respect of which such Person is liable as lessee, (iv) all Operating Lease Obligations of such Person, (v) all Guaranteed Indebtedness, and (vi) all Indebtedness referred to in clause (i), (ii) or (iii) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any Lien upon or in property (including, without limitation, accounts and contract rights) owned by such Person, even though such Person has not assumed or become liable for the payment of such Indebtedness.

"Liens" means, with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind in respect of such asset. For the purposes of

this Agreement, the Company or any Subsidiary shall be deemed to own subject to a Lien any asset which it has acquired or holds subject to the interest of a vendor or lessor under any conditional sale agreement, capital lease or other title retention agreement relating to such asset.

"Material Subsidiary" means at any time a Subsidiary which as of such time meets the definition of a "significant subsidiary" contained as of the date hereof in Regulation S-X of the Securities and Exchange Commission.

"Maximum Credit Amount" means \$45,259,626.31.

"Maximum Drawing Amount" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"Operating Lease Obligations" of any Person means all obligations of such Person as lessee under each operating lease of all or a portion of any Unleased Interests.

"Outstanding Debt" of any Person means at any date, without duplication, (i) all obligations of such Person for borrowed money, (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business, (iv) all obligations of such Person as lessee under capital leases, (v) all Aggregate Operating Lease Obligations of such Person, (vi) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, (vii) all Outstanding Debt of others secured by a Lien on any asset of such Person, whether or not such Outstanding Debt is assumed by such Person, and (viii) all obligations, contingent or otherwise, of such Person directly or indirectly guaranteeing any Outstanding Debt of any other Person or in any manner providing for the payment of any Outstanding Debt of any other Person or otherwise protecting the holder of such Outstanding Debt against loss (whether by agreement to keep-well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), excluding, however, from this clause (viii) endorsements for collection or deposit in the ordinary course of business.

"Participant" has the meaning set forth in Section 14 hereof.

"PBGC" means the Pension Benefit Guaranty Corporation and any entity succeeding to any or all of its functions under ERISA.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" means at any time an employee pension benefit plan which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Code and is either (i) maintained by a member of the Controlled Group for employees of a member of the Controlled Group or (ii) maintained pursuant to a collective bargaining agreement or any other arrangement under which more than one employer makes contributions and to which a member of the Controlled Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions.

"Reimbursement Default" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"Reimbursement Event of Default" has the meaning set forth in Section 9 hereof.

"Subsidiary" means any corporation or other entity of which securities or other ownership interests having ordinary voting power to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by the Company or one or more Subsidiaries, or by the Company and one or more Subsidiaries.

"Successor Participant" means each Person to whom a Participant transfers all or a part of its participation with the consent of the Company.

"Tax" and "Taxes" have the meanings set forth in Section 2(c)(iii) hereof.

"Termination Date" means the earlier of (i) the date on which the Bank pays a drawing under the Letter of Credit for the Maximum Drawing Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of

Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Bank pays such drawing, (iv) the date on which the Company pays the amounts due under Section 9(c) of the Facility Lease, (v) the date on which the Company pays the amounts due under Section 9(d) of the Facility Lease [defaults] or (vi) either (x) the fifth anniversary of the Date of Issuance of the Letter of Credit or (y) if a draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented after 10:00 a.m. but prior to 5:00 p.m. (New York time) on the fifth anniversary of the Date of Issuance of the Letter of Credit, the Business Day following such fifth anniversary.

"Unfunded Vested Liabilities" means, with respect to any Plan at any time, the amount (if any) by which (i) the present value of all vested nonforfeitable benefits under such Plan exceeds (ii) the fair market value of all Plan assets allocable to such benefits, all determined as of the then most recent valuation date for such Plan, but only to the extent that such excess represents a potential liability of a member of the Controlled Group to the PBGC or the Plan under Title IV of ERISA.

"Unit 3" means the 1270 megawatt unit, commonly known as Unit 3, at the Palo Verde Nuclear Generating Station, together with all capital improvements thereto.

"Unleased Interests" means any real or personal or mixed property interest of any Person in that portion of Unit 2 and Unit 3 of the Palo Verde Nuclear Generating Station which is not subject to an operating lease immediately after the Letter of Credit has been issued by the Bank.

(b) Accounting Terms and Determinations. Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Company's independent public accountants) with the most recent audited consolidated financial statements of the Company and its Consolidated Subsidiaries delivered to the Bank.

SECTION 2. Reimbursement. (a) The Company agrees to pay to the Bank (i) not later than 2:00 p.m. New York City

time on the same Business Day on which the Bank shall pay any draft under the Letter of Credit a sum equal to the amount so paid under the Letter of Credit and (ii) interest on any and all amounts unpaid by the Company when due under clause (i) above from and including the date such amount is paid by the Bank under the Letter of Credit until payment in full, payable on demand, at a fluctuating interest rate per annum equal to 2% per annum above the rate of interest publicly announced by the Bank in New York City from time to time as its prime rate, but such fluctuating interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law.

(b) The Company agrees to pay to the Bank (i) a fee with respect to the Letter of Credit equal to .56834% per annum of the Maximum Credit Amount from the Date of Issuance to, but excluding, the Termination Date and (ii) an additional fee computed in accordance with the terms of the letter from the Bank to the Company dated August 1, 1986, in each case payable quarterly in arrears on each February 15, May 15, August 15 and November 15, and on the Termination Date, commencing November 15, 1986, provided that if Moody's Investors Service Inc. ("Moody's") shall rate the debt issued under the Company Indenture lower than Baa3 (or an equivalent rating if the rating system used by Moody's is revised) or Standard & Poor's Corporation ("S&P") shall rate such debt lower than BBB- (or an equivalent rating if the rating system used by S&P is revised), the fee payable pursuant to clause (i) above shall be increased by .15% per annum during the period commencing on the day on which either rating is so lowered to, but excluding, the first day thereafter on which both ratings are at least Baa3 and BBB-, respectively. The Company further agrees to pay to the Bank on the Date of Issuance an initial fee equal to .195% of the Maximum Credit Amount.

(c) (i) If after the date hereof, the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal

Reserve System) against letters of credit issued by or assets of, deposits with or for the account of the Bank or shall impose on the Bank any other condition regarding this Agreement or the Letter of Credit and the result of the foregoing shall be to increase the cost to the Bank of issuing or maintaining the Letter of Credit (which increase in cost shall be the result of the Bank's reasonable allocation of the aggregate of such cost increases resulting from such events), then, within 15 days after demand by the Bank, the Company shall pay to the Bank all additional amounts which are necessary to compensate the Bank for such increased cost incurred by the Bank.

(ii) If after the date hereof, the Bank shall have determined that the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency, has or would have the effect of reducing the rate of return on the Bank's capital as a consequence of its obligations hereunder to a level below that which the Bank could have achieved but for such adoption, change or compliance (taking into consideration the Bank's policies with respect to capital adequacy) by an amount deemed by the Bank to be material, then within 15 days after demand by the Bank, the Company shall pay to the Bank such additional amount or amounts as will compensate the Bank for such reduction.

(iii) All payments made by the Company under this Agreement shall be made free and clear of, and without reduction for or on account of, any stamp or other taxes, levies, imposts, duties, charges, fees, deductions, withholdings, restrictions or conditions of any nature whatsoever hereafter imposed, levied, collected, withheld or assessed by any country (or by any political subdivision or taxing authority thereof or therein), except for franchise taxes and changes in the rate of tax on the overall net income of the Bank (such nonexcluded taxes being called "Tax" or "Taxes"). If any Taxes are required to be withheld from any amounts payable to the Bank, the amounts so payable to the Bank shall be increased to the extent necessary to yield to the Bank (after payment of all Taxes) interest or any such other amounts payable hereunder at the rates or in the amounts specified in this Agreement, provided that the Company shall not be obligated to pay such amounts with respect to any period in

which the Bank has failed (x) to file any form or certificate that it was entitled to file which would have exempted the Bank from such Taxes or (y) to take other action which would entitle the Bank to an exemption from such Taxes, if such action would not, in the reasonable judgement of the Bank, be otherwise disadvantageous to it. Whenever any Tax is payable by the Company, as promptly as possible thereafter, the Company shall send the Bank a receipt or other evidence of payment thereof.

(iv) A certificate as to the nature of the occurrence giving rise to, and the calculation of, compensation to the Bank pursuant to clauses (i), (ii) and (iii) of this Section 2(c) above shall be submitted by the Bank to the Company and shall be conclusive (absent demonstrable error) as to the amount thereof.

(v) The Company agrees that its obligations to pay compensation pursuant to this Section 2(c) shall inure to the benefit of each Participant and each Successor Participant with respect to its respective participation to the same extent as if such Participant or Successor Participant were named instead of the Bank in this Section 2(c), provided that any certificate presented by the Bank on behalf of a Participant or Successor Participant pursuant to Section 2(c) (iv) hereof shall provide the identity of such Participant or Successor Participant and an estimate of the total additional compensation which would be payable to such Participant or Successor Participant on an annual basis.

(vi) No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which the Bank is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by the Bank. No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which a Participant is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by such Participant.

(d) All payments by the Company to the Bank under this Section 2 shall be made in lawful currency of the United States and in immediately available funds at the Bank's principal New York office, which at the date hereof is located at 23 Wall Street, New York, New York 10015, provided that the fee payable under the last sentence of Section 2(b) may be

paid in New York Clearinghouse Funds. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding Business Day, and any interest payable thereon shall be payable for such extended time at the specified rate.

(e) Interest payable under subsection (a) and the fees payable under subsection (b) shall be computed on the basis of a year of 365 days (or 366 days in a leap year) and paid for the actual number of days lapsed (including the first day but excluding the last day).

SECTION 3. Issuance of the Letter of Credit; Conditions Precedent to Issuance. (a) Subject to satisfaction of the conditions precedent set forth in subsections (b), (c) and (d) of this Section, the Bank shall issue the Letter of Credit on the date set forth in the notice referred to in Section 3(b)(viii) hereof (such date or such later date on which the conditions precedent are satisfied and the Letter of Credit is issued being herein called the "Date of Issuance"). The Letter of Credit shall be effective on the Date of Issuance and shall expire on the Termination Date.

(b) As a condition precedent to the issuance of the Letter of Credit, the Bank shall have received on or before the Date of Issuance the following, each dated such date, in form and substance satisfactory to the Bank:

(i) opinions of Snell & Wilmer, counsel for the Company, substantially in the form of Exhibit B hereto;

(ii) opinions of Mudge Rose Guthrie Alexander & Ferdon, special counsel for the Company, substantially in the form of Exhibit C hereto;

(iii) an opinion of Davis Polk & Wardwell, counsel for the Bank, substantially in the form of Exhibit D hereto;

(iv) copies of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance by the Company of this Agreement, each of the Transaction Documents to which the Company is a party and the Collateral Trust Indenture, certified by the Secretary, an Assistant Secretary or an Associate Secretary of the Company (which certificate shall state that such

resolutions are in full force and effect on the Date of Issuance);

(v) certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency required for the Company to enter into this Agreement and of all such approvals, authorizations, orders, consents, notices or registrations required to be obtained or made prior to the Date of Issuance in connection with the transactions contemplated by any of the Transaction Documents or Financing Documents to which the Company is a party;

(vi) a certificate of the Secretary, an Assistant Secretary or an Associate Secretary of the Company certifying the names and true signatures of the officers of the Company authorized to sign this Agreement and the other documents to be delivered by the Company hereunder;

(vii) such other documents, instruments, approvals (and, if requested by the Bank, certified duplicates of executed copies thereof) or opinions as the Bank may reasonably request in writing; and

(viii) receipt by the Bank of a written notice of the proposed Date of Issuance signed by the Company and the Equity Participant.

(c) The following statements shall be true and correct on the Date of Issuance and the Bank shall have received a certificate signed by a duly authorized officer of the Company, dated the Date of Issuance, stating that:

(i) the representations and warranties contained in Section 6 hereof are correct on and as of the Date of Issuance as though made on and as of such date; and

(ii) no Default shall have occurred and be continuing and no Default shall result from the issuance of the Letter of Credit.

(d) On or before the Date of Issuance,

(i) each of the Transaction Documents shall have been duly authorized and executed by the respective parties thereto and shall be in full force and effect;

(ii) the Bank shall have received executed copies (or duplicates thereof) of each Transaction Document, each of which shall be in form and substance satisfactory to the Bank;

(iii) all conditions precedent to the Closing set forth in Section 5(b) of the Participation Agreement shall have been fulfilled; and

(iv) the Purchase Documents shall have been delivered to the Owner Trustee.

SECTION 4. Adjustment of Maximum Drawing Amount; Terms of Drawing. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

SECTION 5. Obligations Absolute. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement, under all circumstances whatsoever, including without limitation the following circumstances:

(a) any lack of validity or enforceability of the Letter of Credit or any of the Transaction Documents or Financing Documents;

(b) any amendment or waiver of or any consent to departure from all or any of the Transaction Documents or Financing Documents;

(c) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant or the Owner Trustee (or any persons or entities for whom any of the foregoing may be acting), the Bank or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents or any unrelated transactions, provided that nothing herein shall prevent the

assertion of any such claim by separate suit or compulsory counterclaim;

(d) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(e) payment by the Bank under the Letter of Credit against presentation of a draft or certificate which does not comply with the terms of such Letter of Credit; or

(f) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

SECTION 6. Representations and Warranties. The Company represents and warrants as follows:

(a) Corporate Existence and Power. The Company is a corporation duly incorporated, validly existing and in good standing under the laws of the State of Arizona, is duly qualified to do business in and is in good standing under the laws of the State of New Mexico and has all corporate powers and all material governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted. All of the issued and outstanding common stock of the Company is owned by AZP Group, Inc.

(b) Corporate Authorization. The execution, delivery and performance by the Company of this Agreement and each Transaction Document and Financing Document (except, for purposes hereof, the Underwriting Agreement) to which it is, or is to become, a party, have been duly authorized by all necessary corporate action on the part of the Company and do not, and will not, require the consent or approval of AZP Group, Inc. or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been, or on or before the Date of Issuance, in the case of the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan, will have been, duly obtained, given or accomplished.

(c) No Violation, etc. Neither the execution, delivery or performance by the Company of this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, nor the consummation by the Company

of the transactions contemplated hereby or thereby, nor compliance by the Company with the provisions hereof or thereof, conflicts or will conflict with, or results or will result in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any indenture, mortgage, lease or any other agreement or instrument to which the Company or any Affiliate of the Company is a party or by which the property of the Company or any Affiliate of the Company is bound, or results or will result in the creation or imposition of any Lien (other than Permitted Liens) upon any property of the Company or any Affiliate of the Company. There is no provision of the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any such indenture, mortgage, lease or other agreement or instrument which materially adversely affects, or in the future is likely (so far as the Company can now foresee) to materially adversely affect, the business, operations, affairs, condition, properties or assets of the Company, or its ability to perform its obligations under this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party.

(d) Governmental Actions. No Governmental Action under any Federal, Arizona or New York law is or will be required in connection with the execution, delivery or performance by the Company of, or the consummation by the Company of the transactions contemplated by, this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of the Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required under existing Federal, Arizona or New York law to be obtained, given or accomplished from time to time after the Date of Issuance in connection with the maintenance, use, possession or operation of Unit 2 or otherwise with respect to Unit 2 and the Company's or the Operating Agent's involvement therewith and which are, for PVNGS, routine in nature and which the Company has no reason to believe will not be timely obtained and (iii) as may be required under Applicable Law not now in effect. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required (a) in

connection with the participation by the Bank or any Participant in the consummation of the transactions contemplated by this Agreement, or in connection with the participation by the Owner Trustee, the Indenture Trustee, the Equity Participant, Funding Corp. or any Loan Participant in the consummation of the transactions contemplated by the Transaction Documents or Financing Documents or (b) to be obtained by any of such Persons during the Lease Term, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan or any Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of any obligations issued under and pursuant to any Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required by existing Applicable Law if, after the Lease Termination Date, the Company should redeliver the Undivided Interest to the Owner Trustee pursuant to Section 5(a) of the Facility Lease or provide transmission services for the Owner Trustee and sell the Retained Assets to the Owner Trustee as provided under the Assignment and Assumption, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person under Section 16 of the Facility Lease.

(e) Execution and Delivery. This Agreement and the Transaction Documents to which the Company is, or is to become, a party on or prior to the Date of Issuance have been or on or before the Date of Issuance will have been duly executed and delivered by the Company, and this Agreement is and upon execution and delivery thereof each such Transaction Document will be the legal, valid and binding obligations of the Company in accordance with their respective terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(f) Litigation. There is no pending action or proceeding before any court, governmental agency or arbitrator against or directly involving the Company or any of its Sub-

sidiaries and, to the best of the Company's knowledge, there is no pending or threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator (A) in which any question is raised as to the validity of this Agreement or any of the Transaction Documents or Financing Documents, or (B) (except as set forth in (i) the Company's Report on Form 10-K for the fiscal year ended December 31, 1985 (the "1985 Form 10-K") in Item 1 thereof under "Rates-State", and "Environmental Requirements"; "Generating Fuel", "Water Supply" and "Indian Matters" or in Item 2 thereof, (ii) the Company's Report on Form 10-Q for the fiscal quarter ended March 31, 1986 in Item 5 thereof under "Retail Rates", "Palo Verde Nuclear Generating Station" and "Environmental Requirements" and (iii) the Company's Report on Form 10-Q for the fiscal quarter ended June 30, 1986 in Item 1 thereof under "Water Supply" and in Item 5 thereof under "Retail Rates" and "Palo Verde Nuclear Generating Station") in which there is any material likelihood of an outcome which may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents. There has been no determination (interim or final) in any action or proceeding so disclosed which determination may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents.

(g) Material Adverse Change. The consolidated balance sheet of the Company and its Consolidated Subsidiaries as at December 31, 1985, and the related consolidated statements of income, of retained earnings and of changes in financial position of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Bank, present fairly the financial position of the Company and its Consolidated Subsidiaries as at such date and the results of the operations of the Company and its Consolidated Subsidiaries for the year ended on such date, in accordance with generally accepted accounting principles consistently applied, and since December 31, 1985, there has been no material adverse change in such position or operations, except as set forth in Appendix A hereto.

(h) Compliance with ERISA. The Company and each member of the Controlled Group have fulfilled their obligations under the minimum funding standards of ERISA and the Code with respect to each Plan (or, with respect to each Plan which is a multiemployer plan as defined in Section 4001(a)(3) of ERISA, have made all required contributions), are in compliance (other than any instance of non-compliance

the liability for which is not material to the Company's or the Controlled Group's financial condition) with the presently applicable provisions of ERISA and the Code, and no events have occurred which have or could result in the imposition of any liability to the PBGC or a Plan under Title IV of ERISA.

SECTION 7. Affirmative Covenants. The Company agrees that during the term of this Agreement it will:

(a) Preservation of Corporate Existence, Etc. (i) Preserve and maintain its corporate existence in the state of its incorporation and qualify and remain qualified as a foreign corporation in each jurisdiction in which such qualification is reasonably necessary in view of its business and operations or the ownership of its properties and (ii) preserve, renew and keep in full force and effect the rights, privileges and franchises necessary or desirable in the normal conduct of its business, except that (a) the Company from time to time makes minor extensions of its system prior to the time a related franchise, certificate, license, or permit is procured, (b) from time to time communities already being served by the Company become incorporated and considerable time may elapse before a franchise is procured, (c) certain franchises may have expired prior to the renegotiation thereof, (d) the Company may not have obtained certain permits or variances relating to the environmental requirements described under "Environmental Requirements" in Item 1 in the 1985 Form 10-K and (e) certain minor defects and exceptions may exist which, individually and in the aggregate, are not deemed material.

(b) Compliance with Laws, Etc. Use its best efforts to comply, and use its best efforts to cause each of its Material Subsidiaries to comply, in all material respects with all applicable laws, rules, regulations, and orders of any governmental authority, the non-compliance with which would materially and adversely affect the business or condition of the Company and its Material Subsidiaries, taken as a whole, such compliance to include, without limitation, paying before the same become delinquent all material taxes, assessments and governmental charges imposed upon it or upon its property, except to the extent compliance with any of the foregoing is then being contested in good faith.

(c) Maintenance of Insurance, Etc. Maintain insurance with responsible and reputable insurance companies or associations or through its own program of self-insurance in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar

properties in the same general areas in which the Company operates and furnish to the Bank within a reasonable time after written request therefor, such information as to the insurance carried as the Bank may reasonably request.

(d) Visitation Rights. At any reasonable time and from time to time, permit the Bank or any agents or representatives thereof to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; provided, however, that the Company reserves the right to restrict access to any of its generating facilities in accordance with reasonably adopted procedures relating to safety and security; and provided, further, that, Section 18 hereof notwithstanding, the costs and expenses incurred by the Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions occurring or made prior to the occurrence of an Event of Default shall be for the account of the Bank. The Bank agrees to use reasonable efforts to ensure that any information concerning the Company or any of its Subsidiaries obtained by the Bank pursuant to this Section which is not contained in a report or other document filed with the Securities and Exchange Commission, distributed by the Company to its security holders or otherwise generally available to the public will, to the extent permitted by law and except as may be required by valid subpoena or in the normal course of the Bank's business operations (which shall include the Bank's sharing of its liability under the Letter of Credit with other banks), be treated confidentially by the Bank and will not be distributed or otherwise made available by the Bank to any Person, other than the Bank's employees, authorized agents or representatives.

(e) Keeping of Books. Keep, and cause each Material Subsidiary to keep, proper books of record and account, in which entries shall be made of all financial transactions and the assets and business of the Company and each Material Subsidiary in accordance with generally accepted accounting principles.

(f) Maintenance of Properties. Maintain and preserve, and cause each Material Subsidiary to maintain and preserve, all of its properties which are used or which are useful in the conduct of its business in good working order and condition, ordinary wear and tear excepted, it being understood that this covenant relates only to the good working

order and condition of such properties and shall not be construed as a covenant of the Company or any Material Subsidiary not to dispose of such properties by sale, lease, transfer or otherwise.

(g) Reporting Requirements. Furnish to the Bank the following: (i) as soon as practicable, and in any event within ten days after the Company knows or has reason to know of the occurrence of a Reimbursement Default which is continuing on the date of such statement, a statement of the chief financial officer (or in his absence, a principal financial officer) of the Company setting forth details of such Reimbursement Default and the action which the Company proposes to take with respect thereto; (ii) as soon as available and in any event within 15 days after filing of each of the Company's Reports on Form 8-K with the Securities and Exchange Commission, a copy of each such report; (iii) as soon as available and in any event within 30 days after filing of each of the Company's Reports on Form 10-Q with the Securities and Exchange Commission, a copy of each such report together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company stating (x) that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (iv) as soon as available and in any event within 30 days after filing of each of the Company's Annual Reports on Form 10-K with the Securities and Exchange Commission, a copy of each such report, together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (v) as soon as available and in any event within 20 days after any member of the Controlled Group (x) gives or is required to give notice to the PBGC of any "reportable event" (as defined in Section 4043 of ERISA) with respect to any Plan which might constitute grounds for the termination of such Plan under Title IV of ERISA, or knows

that the plan administrator of any Plan has given or is required to give notice of any such reportable event, a copy of the notice of such reportable event given or required to be given to the PBGC, provided that no such information need be given with respect to any reportable event for which the 30-day notice requirement of Section 4043(a) of ERISA has been waived, (y) receives notice of complete or partial withdrawal liability under Title IV of ERISA, a copy of such notice or (z) receives notice from the PBGC under the Title IV of ERISA of an intent to terminate or appoint a trustee to administer any Plan, a copy of such notice, (vi) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the Transaction Documents and Financing Documents and (vii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the Company as the Bank may from time to time reasonably request in writing.

(h) Maintenance of Equity. Maintain at all times consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied, of at least \$1.4 billion.

(i) Fixed Charge Ratio. Maintain at all times a Fixed Charge Ratio of at least 2 to 1. "Fixed Charge Ratio" shall mean at any time the ratio of (A) the sum of (x) the consolidated net income of the Company and its Consolidated Subsidiaries for the twelve month period ending with the last month for which the Company has prepared a consolidated income statement, which period shall in no event end earlier than the last day of the month two months prior to the time of the calculation of the Fixed Charge Ratio (the "Twelve Month Period") plus (y) all income taxes deducted in determining said consolidated net income plus (z) the sum of (i) all interest expense in respect of Indebtedness deducted in determining said consolidated net income, (ii) all interest expense in respect of Funded Indebtedness being incurred at the time of calculation of the Fixed Charge Ratio that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate and (iii) all interest expense in respect of Indebtedness other than Funded Indebtedness (I) incurred at any time subsequent to the Twelve Month Period outstanding at the time of the calculation of the Fixed Charge Ratio and (II) being incurred at the time of the calculation of the Fixed Charge Ratio, that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate, (iv) to the extent not covered under clauses

(i), (ii) or (iii) above, (I) rentals payable under Operating Lease Obligations during the Twelve Month Period and (II) with respect to Operating Lease Obligations entered into subsequent to the Twelve Month Period or being entered into at the time of calculation of the Fixed Charge Ratio, the rentals that would have been payable if such Operating Lease Obligations had been outstanding during the Twelve Month Period, provided that rentals payable under any Operating Lease Obligation shall not be included in the calculation of the Fixed Charge Ratio under this clause (iv) until the date that is nine months after the first day of the lease term of such Operating Lease Obligation (the aggregate interest expense and rental payments described in this clause (z) being referred to as the "Interest Expense") to (B) Interest Expense for such period.

SECTION 8. Negative Covenants. The Company agrees that, during the term of this Agreement it will not:

(a) Sales, Etc. of Assets. Sell, lease, transfer or otherwise dispose of (or pledge or otherwise encumber), in any one fiscal year in one or a series of transactions to one or more Persons, including any Subsidiary or Affiliate of the Company, assets with an aggregate value exceeding 10% of the value of the assets of the Company as shown on the consolidated balance sheet of the Company and its Consolidated Subsidiaries included in its audited financial statements for its most recent fiscal year, such assets to be valued on the same basis as that on which they were included in such consolidated financial statements, or, if such assets were not included in such consolidated financial statements, on the same basis as similar assets were valued for such consolidated financial statements, provided, however, that the Company may (i) pledge or encumber assets in connection with the sale of bonds issued under the Company Indenture, (ii) enter into sale and sale-back and sale and lease-back arrangements in connection with Unleased Interests and (iii) create or suffer to exist Excepted Encumbrances as defined in the Company Indenture.

(b) Mergers, Etc. Merge with or into or consolidate with or into any other corporation or entity, or permit any Subsidiary to do so unless (i) immediately after giving effect thereto, no event shall occur and be continuing which constitutes a Reimbursement Default, (ii) the consolidation or merger shall not materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents and (iii) in the case of any merger or consolidation to which the Company is a party, the corporation

formed by such consolidation or into which the Company shall be merged shall assume the Company's obligations under this Agreement in a writing satisfactory in form and substance to the Bank.

(c) Compliance with ERISA. (i) Enter into any prohibited transaction (as defined in Section 4975 of the Internal Revenue Code of 1954, as amended, and in ERISA) involving any Plan which results in any liability of the Company to any Person which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company or (ii) allow or suffer to exist any other event or condition known to the Company which results in any liability of the Company to the PBGC which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company. For purposes of this Section 8(c), "liability" shall not include the contingent liability described in Sections 4201 and 4062 of ERISA or termination insurance premiums payable under Section 4007 of ERISA.

(d) Assignment of Transaction Documents or Financing Documents. After the Date of Issuance, enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents, without first obtaining the express prior written consent of the Bank thereto.

SECTION 9. Reimbursement Events of Default. The following events shall be Reimbursement Events of Default hereunder unless waived by the Bank pursuant to Section 10 hereof:

(i) the Company shall fail to pay when due any amount payable under Section 2 hereunder; or

(ii) the Company shall fail to observe or perform any covenant or agreement contained in this Agreement (other than those covered by clause (i) above or Sections 7(d) and 18 hereof) for 30 days after written notice thereof has been given to the Company by the Bank; or

(iii) any representation, warranty, certification or statement made by the Company in this Agreement or in any certificate, financial statement or other document delivered pursuant to this Agreement shall prove to have been incorrect in any material respect when made; or

(iv) any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) the Company shall (x) fail to make any payment, equal to or exceeding \$5,000,000 of any Outstanding Debt, or to make any payment, equal to or exceeding \$5,000,000, of any interest or premium thereon, when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument relating to the Outstanding Debt, or (y) fail to perform or observe any other term, covenant or condition on its part to be performed or observed under any agreement or instrument relating to any Outstanding Debt when required to be performed or observed, and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure to perform or observe is to accelerate, or to permit the acceleration of, the maturity of any Outstanding Debt, the unpaid principal amount of which then equals or exceeds \$5,000,000; or

(vi) the Company shall (A) apply for or consent to the appointment of a receiver, trustee, liquidator or custodian or the like of itself or of its property, (B) admit in writing its inability to pay its debts generally as they become due, (C) make a general assignment for the benefit of creditors, (D) be adjudicated a bankrupt or insolvent, or (E) commence a voluntary case under the Federal bankruptcy laws of the United States of America or file a voluntary petition or answer seeking reorganization, an arrangement with creditors or any order for relief or seeking to take advantage of any insolvency law or file an answer admitting the material allegations of a petition filed against it in any bankruptcy, reorganization or insolvency proceeding; or corporate action shall be taken by it for the purpose of effecting any of the foregoing, or if without the application, approval or consent

of the Company, a proceeding shall be instituted in any court of competent jurisdiction, seeking in respect of the Company an adjudication in bankruptcy, reorganization, dissolution, winding up, liquidation, a composition or arrangement with creditors, a readjustment of debts, the appointment of a trustee, receiver, liquidator or custodian or the like of the Company or of all or any substantial part of its assets, or other like relief in respect thereof under any bankruptcy or insolvency law, and, if such proceeding is being contested by the Company in good faith, the same shall (i) result in the entry of an order for relief of any such adjudication or appointment or (ii) continue undismissed, or pending and unstayed, for any period of seventy-five (75) consecutive days; or

(vii) any judgment or order for the payment of money exceeding any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and either (i) enforcement proceedings shall have been commenced by any creditor upon such judgment or order or (ii) there shall be any period of ten consecutive days during which a stay of enforcement of such judgment or order, by reason of a pending appeal or otherwise, shall not be in effect; or

(viii) the Company or any member of the Controlled Group shall fail to pay when due an amount or amounts aggregating in excess of \$5,000,000 which it shall have become liable to pay to the PBGC or to a Plan under Title IV of ERISA; or notice of intent to terminate a Plan or Plans having aggregate Unfunded Vested Liabilities in excess of \$10,000,000 (collectively a "Material Plan") shall be filed under Title IV of ERISA by the Company, any member of the Controlled Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate or to cause a trustee to be appointed to administer any Material Plan; or a proceeding shall be instituted by a fiduciary of any Material Plan against the Company or any member of the Controlled Group to enforce Section 515 of ERISA in which the amount in controversy exceeds \$1,000,000 and such proceeding shall not have been dismissed within 30 days thereafter; or a condition shall exist by reason of which the PBGC would be entitled under

Title IV of ERISA to obtain a decree adjudicating that any Material Plan must be terminated; or

(ix) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(x) any event specified in Sections 15 (vii), (viii) or (x) of the Facility Lease shall occur; or

(xi) the Company shall fail to make, or cause to be made, any payment specified in Section 15 (i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

If an Event of Default occurs and is continuing, the Bank may, in its sole discretion by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein.

SECTION 10. Amendments and Waivers. No amendment or waiver of any provision of this Agreement, nor consent to any departure by the Company therefrom nor any consent to the assignment of the Company's obligations under the Transaction Documents or the Financing Documents shall in any event be effective unless the same shall be in writing and signed by the Bank. Any such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given.

SECTION 11. Notices. All notices, requests and other communications to any party hereunder shall be in writing (including telex or similar writing) and shall be given to such party, addressed to it, at its address or telex number set forth below or such other address or telex number as such party may hereafter specify for the purpose by notice to the other party. Each such notice, request or communication shall be effective (i) if given by telex, when such telex is transmitted to the telex number specified below and the appropriate answerback is received, (ii) if given by mail upon receipt but not later than 10 days after such communication is deposited in the mails with first class postage prepaid, addressed as aforesaid or (iii) if given by any other means, when delivered at the address specified below.

Party
Arizona Public Service
Company

Address
Street Address:
411 North Central Avenue
Phoenix, Arizona 85004

Mailing Address:
P.O. Box 53999
Phoenix, Arizona 85072-3999
Attention: Treasurer
Telex: TWX165232
Answerback: APS PHNX
Facsimile Transmission:
(602) 250-2061

Morgan Guaranty Trust
Company of New York

150 William Street
17th Floor
New York, New York 10015
Attn: Letter of Credit
Department
(Copy to
Utilities Department)
Telex: 420230
Answerback: MGT UI
or
Telex: 232194
Answerback: MGT UR
Facsimile Transmission:
(212) 344-9454

SECTION 12. No Waiver; Remedies. No failure on the part of the Bank to exercise, and no delay in exercising, any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise of any right hereunder preclude any other further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

SECTION 13. Waiver of Right of Setoff. The Bank hereby waives any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by the Bank to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up,

reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "bankruptcy events"), against any and all of the obligations of the Company now or hereafter existing in respect of the reimbursement obligation of the Company set forth in Section 2(a) hereof, provided any such waiver shall be deemed ineffective as and to the extent that the Bank receives, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience, (which counsel shall be mutually satisfactory to the Bank and the Owner Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section.

SECTION 14. Sales of Participations. The Bank may grant participations under this Agreement and the Letters of Credit (each person to which a participation is granted being called a "Participant") and in such event the Bank will in its own name and as agent for any Participant, enforce all rights and interests of any Participant under this Agreement, and accept all performances required of the Company under this Agreement, provided that (i) the Bank shall not agree to a substitution or replacement of a Participant or a change in the proportionate amount of any Participant's participation after the Date of Issuance unless the Bank shall have received the Company's prior written consent thereto, which consent shall not be unreasonably withheld and (ii) in the event that a claim for compensation is made pursuant to Section 2(c) on behalf of a Participant, the Company shall have the right, with the assistance of the Bank, to seek a substitute participant or participants, satisfactory to the Bank, to assume the participation of such Participant.

SECTION 15. Continuing Obligation. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date or (ii) the date upon which all amounts due and owing to the Bank hereunder shall have been paid in full and shall (a) be binding upon the Company

and its successors and assigns and (b) inure to the benefit of and be enforceable by the Bank and its successors, transferees and assigns, provided, however, that the Company may not assign all or any part of this Agreement without the prior written consent of the Bank.

SECTION 16. Extension of Letter of Credit. At least 90 but not more than 180 days before the fifth anniversary of the Date of Issuance, the Company may request the Bank in writing to extend for not less than three years, nor more than eight years, the Termination Date of the Letter of Credit, specifying the terms and conditions, including fees, to be applicable to such extension. No later than 30 days from the date on which the Bank shall have received notice from the Company pursuant to the preceding sentence, the Bank shall notify the Company of its consent or nonconsent to such extension request, and if the Bank shall give no such notice, the Bank shall be deemed not to have consented to such extension request. The Bank's consent shall be conditional upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to the Bank and its counsel incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement between the Company and the Bank.

SECTION 17. Limited Liability of the Bank. The Company assumes all risks of the acts or omissions of the Equity Participant with respect to its use of the Letter of Credit. Neither the Bank nor any of its officers or directors shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or for any acts or omissions of the Equity Participant in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement(s) thereon, even if such documents should in fact prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except only that the Company shall have a claim against the Bank, and the Bank shall be liable to the Company to the extent, but only to the extent, of any direct, as opposed to consequential, damages suffered by the Company which the Company proves were caused by (i) the Bank's willful misconduct or gross negligence in determining whether documents presented under the Letter of Credit comply with the terms thereof or (ii) the Bank's willful failure to pay under the Letter of Credit after the

presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. In furtherance and not in limitation of the foregoing, the Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

SECTION 18. Costs, Expenses and Taxes. The Company agrees to pay not later than 30 days after demand therefor all reasonable costs and expenses in connection with the preparation, execution, delivery, filing and administration of this Agreement and any other documents which may be delivered in connection with this Agreement, including, without limitation, the reasonable fees and out-of-pocket expenses of counsel for the Bank with respect thereto and with respect to advising the Bank as to its rights and responsibilities under this Agreement or any waiver or amendment of, or the enforcement of, this Agreement and such other documents which may be delivered in connection with this Agreement. In addition, the Company shall pay any and all stamp and other taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents and agrees to save the Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, provided that the Bank agrees promptly to notify the Company of any such taxes and fees which are incurred by the Bank.

SECTION 19. Indemnification. The Company hereby agrees to indemnify and hold harmless the Bank from and against any and all claims, damages, losses, liabilities, costs or expenses whatsoever which the Bank may incur (or which may be claimed against the Bank by any person or entity whatsoever). (i) by reason of any inaccuracy in any material respect, or untrue statement or alleged untrue statement of any material fact contained or incorporated by reference in any offering document distributed by or on behalf of the Company in connection with obtaining purchasers of the Company's undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station, or in any supplement or amendment to either thereof, or the omission or alleged omission to state therein a material fact necessary to make such statements, in the light of the circumstances under which they are or were made, not misleading; (ii) by reason of or in connection with

the execution, delivery and performance of the Transaction Documents and Financing Documents; or (iii) by reason of or in connection with the execution and delivery or transfer of, or payment or failure to make lawful payment under, the Letter of Credit; provided that the Company shall not be required to indemnify the Bank for any claims, damages, losses, liabilities, costs or expenses to the extent, but only to the extent, caused by the willful misconduct or gross negligence of the Bank in determining whether a draft or certificate presented under the Letter of Credit complied with the terms of the Letter of Credit or the Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. Nothing in this Section 19 is intended to limit the Company's reimbursement obligation contained in paragraph (a) of Section 2 hereof. Without prejudice to the survival of any other obligation of the Company hereunder, the indemnitees and obligations of the Company contained in this Section 19 shall survive the payment in full of amounts payable under Section 2 and the termination of the Letter of Credit.

SECTION 20. Severability. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

SECTION 21. Governing Law. This Agreement shall be governed by, and construed and interpreted in accordance with, the laws of the State of New York.

SECTION 22. Headings. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By *J. H. Miller*

Title:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK

By *David A. Belcher*

Title: *Vice President*

IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. S-1001

August 18, 1986

Security Pacific Capital
Leasing Corporation
Four Embarcadero Center
Suite 1200
San Francisco, California 94111

Attn: Chief Counsel
Manager - Lease Investments
Manager - Lease Services

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "Company"), in your favor, our Irrevocable Transferable Letter of Credit No. S-1001 (the "Letter of Credit"), in an amount not to exceed \$45,259,626.31 (the "Maximum Credit Amount"), effective immediately and expiring at 5:00 p.m. (New York time) on the Termination Date. Capitalized terms used herein and in Schedules II and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "Facility Lease") between the Company and the First National Bank of Boston, as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "Date of Drawing") in the Table of Maximum Drawing Amounts attached hereto as Schedule II as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next paragraph, are hereinafter referred to collectively as the "Maximum Drawing Amounts" and

REIMBURSEMENT AGREEMENT

between

Arizona Public Service Company

and

Morgan Guaranty Trust Company of New York

dated as of

August 1, 1986

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REIMBURSEMENT AGREEMENT

REIMBURSEMENT AGREEMENT, dated as of August 1, 1986 between Arizona Public Service Company, an Arizona corporation (the "Company"), and MORGAN GUARANTY TRUST COMPANY OF NEW YORK (the "Bank").

WHEREAS, the Company has entered into a Participation Agreement dated as of August 1, 1986 among the Company, The First National Bank of Boston, for itself and as Owner Trustee (the "Owner Trustee"), Chemical Bank, for itself and as Indenture Trustee, Bank of America National Trust and Savings Association, for itself and as Agent for the Loan Participants, PVNGS Funding Corp, Inc. and Security Pacific Capital Leasing Corporation, as Equity Participant (the "Equity Participant") relating to the acquisition of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station through a trust for the benefit of the Equity Participant which interest will be leased to the Company pursuant to a lease dated as of August 1, 1986 between the Owner Trustee and the Company (the "Facility Lease"); and

WHEREAS, it is a condition precedent to the Owner Trustee's making available, on behalf of the Equity Participant, the Purchase Price of Unit 2 that the Bank issue to the Equity Participant an irrevocable letter of credit in the form of Exhibit A hereto (the "Letter of Credit"); and

WHEREAS, the Bank is willing to issue the Letter of Credit on the terms and subject to the conditions set forth in this Agreement;

NOW, THEREFORE, the Bank and the Company hereby agree as follows:

SECTION 1. (a) Definitions. Capitalized terms used herein and not otherwise defined herein shall have the respective meanings assigned thereto in Appendix A to the Facility Lease. The following terms, as used herein, have the following respective meanings:

"Aggregate Operating Lease Obligations" of any Person means all Operating Lease Obligations under operating leases which are entered into by such Person in substantially contemporaneous transactions.

"Agreement" means this Reimbursement Agreement, as the same may from time to time be amended, supplemented or modified.

"Business Day" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close.

"Code" means the United States Internal Revenue Code of 1954, as amended.

"Company Indenture" means the Mortgage and Deed of Trust dated as of July 1, 1946, as amended and supplemented at the date hereof, of Central Arizona Light and Power Company (now the Company) to Security-First National Bank of Los Angeles (now Security Pacific National Bank), as Trustee.

"Controlled Group" means all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Company, are treated as a single employer under Section 414(b) or 414(c) of the Code.

"Consolidated Subsidiary" means at any date any subsidiary or other entity the accounts of which would be consolidated with those of the Company in the Company's consolidated financial statements as of such date.

"Date of Early Termination" has the meaning set forth in the Letter of Credit.

"Date of Issuance" means the date on which the Letter of Credit is issued upon request of the Company pursuant to Section 3(a) hereof.

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

"Fixed Charge Ratio" has the meaning set forth in Section 7(i) hereof.

"Funded Indebtedness" means all Indebtedness which matures more than one year from the date of its creation or matures within one year from such date but is renewable or extendible, at the option of the Company, to a date more than one year from such date or arises under a revolving credit or similar agreement which obligates the lender or lenders to extend credit during a period of more than one year from such

date including, without limitation, all amounts of Funded Indebtedness required to be paid or prepaid within one year from the date of its creation.

"Guaranteed Indebtedness" of any Person means all Indebtedness referred to in clause (i), (ii) or (iii) of the definition of "Indebtedness" guaranteed directly or indirectly in any manner by such Person, or in effect guaranteed directly or indirectly by such Person through an agreement (i) to pay or purchase such Indebtedness or to advance or supply funds for the payment or purchase of such Indebtedness, or (ii) to purchase, sell or lease (as lessee or lessor) property, or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such Indebtedness or to assure the holder of such Indebtedness against loss, or (iii) to supply funds to or in any other manner invest in the debtor (including any agreement to pay for property or services irrespective of whether or not such property is received or such services are rendered), or (iv) otherwise to assure a creditor against loss.

"Imputed Rate" means, in respect of Indebtedness, the actual initial rate of interest to be paid by a Person with respect to such Indebtedness.

"Indebtedness" of any Person means (i) all indebtedness of such Person for borrowed money or for the deferred purchase price of property or services, (ii) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property acquired by such Person (even though the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property), (iii) all obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, recorded as capital leases in respect of which such Person is liable as lessee, (iv) all Operating Lease Obligations of such Person, (v) all Guaranteed Indebtedness, and (vi), all Indebtedness referred to in clause (i), (ii) or (iii) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any Lien upon or in property (including, without limitation, accounts and contract rights) owned by such Person, even though such Person has not assumed or become liable for the payment of such Indebtedness.

"Liens" means, with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind in respect of such asset. For the purposes of

this Agreement, the Company or any Subsidiary shall be deemed to own subject to a Lien any asset which it has acquired or holds subject to the interest of a vendor or lessor under any conditional sale agreement, capital lease or other title retention agreement relating to such asset.

"Material Subsidiary" means at any time a Subsidiary which as of such time meets the definition of a "significant subsidiary" contained as of the date hereof in Regulation S-X of the Securities and Exchange Commission.

"Maximum Credit Amount" means \$45,259,626.31.

"Maximum Drawing Amount" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"Operating Lease Obligations" of any Person means all obligations of such Person as lessee under each operating lease of all or a portion of any Unleased Interests.

"Outstanding Debt" of any Person means at any date, without duplication, (i) all obligations of such Person for borrowed money, (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business, (iv) all obligations of such Person as lessee under capital leases, (v) all Aggregate Operating Lease Obligations of such Person, (vi) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, (vii) all Outstanding Debt of others secured by a Lien on any asset of such Person, whether or not such Outstanding Debt is assumed by such Person, and (viii) all obligations, contingent or otherwise, of such Person directly or indirectly guaranteeing any Outstanding Debt of any other Person or in any manner providing for the payment of any Outstanding Debt of any other Person or otherwise protecting the holder of such Outstanding Debt against loss (whether by agreement to keep-well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), excluding, however, from this clause (viii) endorsements for collection or deposit in the ordinary course of business.

"Participant" has the meaning set forth in Section 14 hereof.

"PBGC" means the Pension Benefit Guaranty Corporation and any entity succeeding to any or all of its functions under ERISA.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" means at any time an employee pension benefit plan which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Code and is either (i) maintained by a member of the Controlled Group for employees of a member of the Controlled Group or (ii) maintained pursuant to a collective bargaining agreement or any other arrangement under which more than one employer makes contributions and to which a member of the Controlled Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions.

"Reimbursement Default" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"Reimbursement Event of Default" has the meaning set forth in Section 9 hereof.

"Subsidiary" means any corporation or other entity of which securities or other ownership interests having ordinary voting power to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by the Company or one or more Subsidiaries, or by the Company and one or more Subsidiaries.

"Successor Participant" means each Person to whom a Participant transfers all or a part of its participation with the consent of the Company.

"Tax" and "Taxes" have the meanings set forth in Section 2(c)(iii) hereof.

"Termination Date" means the earlier of (i) the date on which the Bank pays a drawing under the Letter of Credit for the Maximum Drawing Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of

Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Bank pays such drawing, (iv) the date on which the Company pays the amounts due under Section 9(c) of the Facility Lease, (v) the date on which the Company pays the amounts due under Section 9(d) of the Facility Lease [defaults] or (vi) either (x) the fifth anniversary of the Date of Issuance of the Letter of Credit or (y) if a draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented after 10:00 a.m. but prior to 5:00 p.m. (New York time) on the fifth anniversary of the Date of Issuance of the Letter of Credit, the Business Day following such fifth anniversary.

"Unfunded Vested Liabilities" means, with respect to any Plan at any time, the amount (if any) by which (i) the present value of all vested nonforfeitable benefits under such Plan exceeds (ii) the fair market value of all Plan assets allocable to such benefits, all determined as of the then most recent valuation date for such Plan, but only to the extent that such excess represents a potential liability of a member of the Controlled Group to the PBGC or the Plan under Title IV of ERISA.

"Unit 3" means the 1270 megawatt unit, commonly known as Unit 3, at the Palo Verde Nuclear Generating Station, together with all capital improvements thereto.

"Unleased Interests" means any real or personal or mixed property interest of any Person in that portion of Unit 2 and Unit 3 of the Palo Verde Nuclear Generating Station which is not subject to an operating lease immediately after the Letter of Credit has been issued by the Bank.

(b) Accounting Terms and Determinations. Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Company's independent public accountants) with the most recent audited consolidated financial statements of the Company and its Consolidated Subsidiaries delivered to the Bank.

SECTION 2. Reimbursement. (a) The Company agrees to pay to the Bank (i) not later than 2:00 p.m. New York City

time on the same Business Day on which the Bank shall pay any draft under the Letter of Credit a sum equal to the amount so paid under the Letter of Credit and (ii) interest on any and all amounts unpaid by the Company when due under clause (i) above from and including the date such amount is paid by the Bank under the Letter of Credit until payment in full, payable on demand, at a fluctuating interest rate per annum equal to 2% per annum above the rate of interest publicly announced by the Bank in New York City from time to time as its prime rate, but such fluctuating interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law.

(b) The Company agrees to pay to the Bank (i) a fee with respect to the Letter of Credit equal to .56834% per annum of the Maximum Credit Amount from the Date of Issuance to, but excluding, the Termination Date and (ii) an additional fee computed in accordance with the terms of the letter from the Bank to the Company dated August 1, 1986, in each case payable quarterly in arrears on each February 15, May 15, August 15 and November 15, and on the Termination Date, commencing November 15, 1986, provided that if Moody's Investors Service Inc. ("Moody's") shall rate the debt issued under the Company Indenture lower than Baa3 (or an equivalent rating if the rating system used by Moody's is revised) or Standard & Poor's Corporation ("S&P") shall rate such debt lower than BBB- (or an equivalent rating if the rating system used by S&P is revised), the fee payable pursuant to clause (i) above shall be increased by .15% per annum during the period commencing on the day on which either rating is so lowered to, but excluding, the first day thereafter on which both ratings are at least Baa3 and BBB-, respectively. The Company further agrees to pay to the Bank on the Date of Issuance an initial fee equal to .195% of the Maximum Credit Amount.

(c) (i) If after the date hereof, the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal

Reserve System) against letters of credit issued by or assets of, deposits with or for the account of the Bank or shall impose on the Bank any other condition regarding this Agreement or the Letter of Credit and the result of the foregoing shall be to increase the cost to the Bank of issuing or maintaining the Letter of Credit (which increase in cost shall be the result of the Bank's reasonable allocation of the aggregate of such cost increases resulting from such events), then, within 15 days after demand by the Bank, the Company shall pay to the Bank all additional amounts which are necessary to compensate the Bank for such increased cost incurred by the Bank.

(ii) If after the date hereof, the Bank shall have determined that the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency, has or would have the effect of reducing the rate of return on the Bank's capital as a consequence of its obligations hereunder to a level below that which the Bank could have achieved but for such adoption, change or compliance (taking into consideration the Bank's policies with respect to capital adequacy) by an amount deemed by the Bank to be material, then within 15 days after demand by the Bank, the Company shall pay to the Bank such additional amount or amounts as will compensate the Bank for such reduction.

(iii) All payments made by the Company under this Agreement shall be made free and clear of, and without reduction for or on account of, any stamp or other taxes, levies, imposts, duties, charges, fees, deductions, withholdings, restrictions or conditions of any nature whatsoever hereafter imposed, levied, collected, withheld or assessed by any country (or by any political subdivision or taxing authority thereof or therein), except for franchise taxes and changes in the rate of tax on the overall net income of the Bank (such nonexcluded taxes being called "Tax" or "Taxes"). If any Taxes are required to be withheld from any amounts payable to the Bank, the amounts so payable to the Bank shall be increased to the extent necessary to yield to the Bank (after payment of all Taxes) interest or any such other amounts payable hereunder at the rates or in the amounts specified in this Agreement, provided that the Company shall not be obligated to pay such amounts with respect to any period in

which the Bank has failed (x) to file any form or certificate that it was entitled to file which would have exempted the Bank from such Taxes or (y) to take other action which would entitle the Bank to an exemption from such Taxes, if such action would not, in the reasonable judgement of the Bank, be otherwise disadvantageous to it. Whenever any Tax is payable by the Company, as promptly as possible thereafter, the Company shall send the Bank a receipt or other evidence of payment thereof.

(iv) A certificate as to the nature of the occurrence giving rise to, and the calculation of, compensation to the Bank pursuant to clauses (i), (ii) and (iii) of this Section 2(c) above shall be submitted by the Bank to the Company and shall be conclusive (absent demonstrable error) as to the amount thereof.

(v) The Company agrees that its obligations to pay compensation pursuant to this Section 2(c) shall inure to the benefit of each Participant and each Successor Participant with respect to its respective participation to the same extent as if such Participant or Successor Participant were named instead of the Bank in this Section 2(c), provided that any certificate presented by the Bank on behalf of a Participant or Successor Participant pursuant to Section 2(c)(iv) hereof shall provide the identity of such Participant or Successor Participant and an estimate of the total additional compensation which would be payable to such Participant or Successor Participant on an annual basis.

(vi) No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which the Bank is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by the Bank. No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which a Participant is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by such Participant.

(d) All payments by the Company to the Bank under this Section 2 shall be made in lawful currency of the United States and in immediately available funds at the Bank's principal New York office, which at the date hereof is located at 23 Wall Street, New York, New York 10015, provided that the fee payable under the last sentence of Section 2(b) may be

paid in New York Clearinghouse Funds. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding Business Day, and any interest payable thereon shall be payable for such extended time at the specified rate.

(e) Interest payable under subsection (a) and the fees payable under subsection (b) shall be computed on the basis of a year of 365 days (or 366 days in a leap year) and paid for the actual number of days lapsed (including the first day but excluding the last day).

SECTION 3. Issuance of the Letter of Credit; Conditions Precedent to Issuance. (a) Subject to satisfaction of the conditions precedent set forth in subsections (b), (c) and (d) of this Section, the Bank shall issue the Letter of Credit on the date set forth in the notice referred to in Section 3(b)(viii) hereof (such date or such later date on which the conditions precedent are satisfied and the Letter of Credit is issued being herein called the "Date of Issuance"). The Letter of Credit shall be effective on the Date of Issuance and shall expire on the Termination Date.

(b) As a condition precedent to the issuance of the Letter of Credit, the Bank shall have received on or before the Date of Issuance the following, each dated such date, in form and substance satisfactory to the Bank:

(i) opinions of Snell & Wilmer, counsel for the Company, substantially in the form of Exhibit B hereto;

(ii) opinions of Mudge Rose Guthrie Alexander & Ferdon, special counsel for the Company, substantially in the form of Exhibit C hereto;

(iii) an opinion of Davis Polk & Wardwell, counsel for the Bank, substantially in the form of Exhibit D hereto;

(iv) copies of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance by the Company of this Agreement, each of the Transaction Documents to which the Company is a party and the Collateral Trust Indenture, certified by the Secretary, an Assistant Secretary or an Associate Secretary of the Company (which certificate shall state that such

resolutions are in full force and effect on the Date of Issuance);

(v) certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency required for the Company to enter into this Agreement and of all such approvals, authorizations, orders, consents, notices or registrations required to be obtained or made prior to the Date of Issuance in connection with the transactions contemplated by any of the Transaction Documents or Financing Documents to which the Company is a party;

(vi) a certificate of the Secretary, an Assistant Secretary or an Associate Secretary of the Company certifying the names and true signatures of the officers of the Company authorized to sign this Agreement and the other documents to be delivered by the Company hereunder;

(vii) such other documents, instruments, approvals (and, if requested by the Bank, certified duplicates of executed copies thereof) or opinions as the Bank may reasonably request in writing; and

(viii) receipt by the Bank of a written notice of the proposed Date of Issuance signed by the Company and the Equity Participant.

(c) The following statements shall be true and correct on the Date of Issuance and the Bank shall have received a certificate signed by a duly authorized officer of the Company, dated the Date of Issuance, stating that:

(i) the representations and warranties contained in Section 6 hereof are correct on and as of the Date of Issuance as though made on and as of such date; and

(ii) no Default shall have occurred and be continuing and no Default shall result from the issuance of the Letter of Credit.

(d) On or before the Date of Issuance,

(i) each of the Transaction Documents shall have been duly authorized and executed by the respective parties thereto and shall be in full force and effect;

(ii) the Bank shall have received executed copies (or duplicates thereof) of each Transaction Document, each of which shall be in form and substance satisfactory to the Bank;

(iii) all conditions precedent to the Closing set forth in Section 5(b) of the Participation Agreement shall have been fulfilled; and

(iv) the Purchase Documents shall have been delivered to the Owner Trustee.

SECTION 4. Adjustment of Maximum Drawing Amount; Terms of Drawing. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

SECTION 5. Obligations Absolute. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement, under all circumstances whatsoever, including without limitation the following circumstances:

(a) any lack of validity or enforceability of the Letter of Credit or any of the Transaction Documents or Financing Documents;

(b) any amendment or waiver of or any consent to departure from all or any of the Transaction Documents or Financing Documents;

(c) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant or the Owner Trustee (or any persons or entities for whom any of the foregoing may be acting), the Bank or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents or any unrelated transactions, provided that nothing herein shall prevent the

assertion of any such claim by separate suit or compulsory counterclaim;

(d) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(e) payment by the Bank under the Letter of Credit against presentation of a draft or certificate which does not comply with the terms of such Letter of Credit; or

(f) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

SECTION 6. Representations and Warranties. The Company represents and warrants as follows:

(a) Corporate Existence and Power. The Company is a corporation duly incorporated, validly existing and in good standing under the laws of the State of Arizona, is duly qualified to do business in and is in good standing under the laws of the State of New Mexico and has all corporate powers and all material governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted. All of the issued and outstanding common stock of the Company is owned by AZP Group, Inc.

(b) Corporate Authorization. The execution, delivery and performance by the Company of this Agreement and each Transaction Document and Financing Document (except, for purposes hereof, the Underwriting Agreement) to which it is, or is to become, a party, have been duly authorized by all necessary corporate action on the part of the Company and do not, and will not, require the consent or approval of AZP Group, Inc. or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been, or on or before the Date of Issuance, in the case of the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan, will have been, duly obtained, given or accomplished.

(c) No Violation, etc. Neither the execution, delivery or performance by the Company of this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, nor the consummation by the Company

of the transactions contemplated hereby or thereby, nor compliance by the Company with the provisions hereof or thereof, conflicts or will conflict with, or results or will result in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any indenture, mortgage, lease or any other agreement or instrument to which the Company or any Affiliate of the Company is a party or by which the property of the Company or any Affiliate of the Company is bound, or results or will result in the creation or imposition of any Lien (other than Permitted Liens) upon any property of the Company or any Affiliate of the Company. There is no provision of the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any such indenture, mortgage, lease or other agreement or instrument which materially adversely affects, or in the future is likely (so far as the Company can now foresee) to materially adversely affect, the business, operations, affairs, condition, properties or assets of the Company, or its ability to perform its obligations under this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party.

(d) Governmental Actions. No Governmental Action under any Federal, Arizona or New York law is or will be required in connection with the execution, delivery or performance by the Company of, or the consummation by the Company of the transactions contemplated by, this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of the Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required under existing Federal, Arizona or New York law to be obtained, given or accomplished from time to time after the Date of Issuance in connection with the maintenance, use, possession or operation of Unit 2 or otherwise with respect to Unit 2 and the Company's or the Operating Agent's involvement therewith and which are, for PVNGS, routine in nature and which the Company has no reason to believe will not be timely obtained and (iii) as may be required under Applicable Law not now in effect. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required (a) in

connection with the participation by the Bank or any Participant in the consummation of the transactions contemplated by this Agreement, or in connection with the participation by the Owner Trustee, the Indenture Trustee, the Equity Participant, Funding Corp. or any Loan Participant in the consummation of the transactions contemplated by the Transaction Documents or Financing Documents or (b) to be obtained by any of such Persons during the Lease Term, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan or any Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of any obligations issued under and pursuant to any Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required by existing Applicable Law if, after the Lease Termination Date, the Company should redeliver the Undivided Interest to the Owner Trustee pursuant to Section 5(a) of the Facility Lease or provide transmission services for the Owner Trustee and sell the Retained Assets to the Owner Trustee as provided under the Assignment and Assumption, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person under Section 16 of the Facility Lease.

(e) Execution and Delivery. This Agreement and the Transaction Documents to which the Company is, or is to become, a party on or prior to the Date of Issuance have been or on or before the Date of Issuance will have been duly executed and delivered by the Company, and this Agreement is and upon execution and delivery thereof each such Transaction Document will be the legal, valid and binding obligations of the Company in accordance with their respective terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(f) Litigation. There is no pending action or proceeding before any court, governmental agency or arbitrator against or directly involving the Company or any of its Sub-

sidiaries and, to the best of the Company's knowledge, there is no pending or threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator (A) in which any question is raised as to the validity of this Agreement or any of the Transaction Documents or Financing Documents, or (B) (except as set forth in (i) the Company's Report on Form 10-K for the fiscal year ended December 31, 1985 (the "1985 Form 10-K") in Item 1 thereof under "Rates-State", and "Environmental Requirements", "Generating Fuel", "Water Supply" and "Indian Matters" or in Item 2 thereof, (ii) the Company's Report on Form 10-Q for the fiscal quarter ended March 31, 1986 in Item 5 thereof under "Retail Rates", "Palo Verde Nuclear Generating Station" and "Environmental Requirements" and (iii) the Company's Report on Form 10-Q for the fiscal quarter ended June 30, 1986 in Item 1 thereof under "Water Supply" and in Item 5 thereof under "Retail Rates" and "Palo Verde Nuclear Generating Station") in which there is any material likelihood of an outcome which may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents. There has been no determination (interim or final) in any action or proceeding so disclosed which determination may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents.

(g) Material Adverse Change. The consolidated balance sheet of the Company and its Consolidated Subsidiaries as at December 31, 1985, and the related consolidated statements of income, of retained earnings and of changes in financial position of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Bank, present fairly the financial position of the Company and its Consolidated Subsidiaries as at such date and the results of the operations of the Company and its Consolidated Subsidiaries for the year ended on such date, in accordance with generally accepted accounting principles consistently applied, and since December 31, 1985, there has been no material adverse change in such position or operations, except as set forth in Appendix A hereto.

(h) Compliance with ERISA. The Company and each member of the Controlled Group have fulfilled their obligations under the minimum funding standards of ERISA and the Code with respect to each Plan (or, with respect to each Plan which is a multiemployer plan as defined in Section 4001(a)(3) of ERISA, have made all required contributions), are in compliance (other than any instance of non-compliance

the liability for which is not material to the Company's or the Controlled Group's financial condition) with the presently applicable provisions of ERISA and the Code, and no events have occurred which have or could result in the imposition of any liability to the PBGC or a Plan under Title IV of ERISA.

SECTION 7. Affirmative Covenants. The Company agrees that during the term of this Agreement it will:

(a) Preservation of Corporate Existence, Etc. (i) Preserve and maintain its corporate existence in the state of its incorporation and qualify and remain qualified as a foreign corporation in each jurisdiction in which such qualification is reasonably necessary in view of its business and operations or the ownership of its properties and (ii) preserve, renew and keep in full force and effect the rights, privileges and franchises necessary or desirable in the normal conduct of its business, except that (a) the Company from time to time makes minor extensions of its system prior to the time a related franchise, certificate, license, or permit is procured, (b) from time to time communities already being served by the Company become incorporated and considerable time may elapse before a franchise is procured, (c) certain franchises may have expired prior to the renegotiation thereof, (d) the Company may not have obtained certain permits or variances relating to the environmental requirements described under "Environmental Requirements" in Item 1 in the 1985 Form 10-K and (e) certain minor defects and exceptions may exist which, individually and in the aggregate, are not deemed material.

(b) Compliance with Laws, Etc. Use its best efforts to comply, and use its best efforts to cause each of its Material Subsidiaries to comply, in all material respects with all applicable laws, rules, regulations, and orders of any governmental authority, the non-compliance with which would materially and adversely affect the business or condition of the Company and its Material Subsidiaries, taken as a whole, such compliance to include, without limitation, paying before the same become delinquent all material taxes, assessments and governmental charges imposed upon it or upon its property, except to the extent compliance with any of the foregoing is then being contested in good faith.

(c) Maintenance of Insurance, Etc. Maintain insurance with responsible and reputable insurance companies or associations or through its own program of self-insurance in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar

properties in the same general areas in which the Company operates and furnish to the Bank within a reasonable time after written request therefor, such information as to the insurance carried as the Bank may reasonably request.

(d) Visitation Rights. At any reasonable time and from time to time, permit the Bank or any agents or representatives thereof to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; provided, however, that the Company reserves the right to restrict access to any of its generating facilities in accordance with reasonably adopted procedures relating to safety and security; and provided, further, that, Section 18 hereof notwithstanding, the costs and expenses incurred by the Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions occurring or made prior to the occurrence of an Event of Default shall be for the account of the Bank. The Bank agrees to use reasonable efforts to ensure that any information concerning the Company or any of its Subsidiaries obtained by the Bank pursuant to this Section which is not contained in a report or other document filed with the Securities and Exchange Commission, distributed by the Company to its security holders or otherwise generally available to the public will, to the extent permitted by law and except as may be required by valid subpoena or in the normal course of the Bank's business operations (which shall include the Bank's sharing of its liability under the Letter of Credit with other banks), be treated confidentially by the Bank and will not be distributed or otherwise made available by the Bank to any Person, other than the Bank's employees, authorized agents or representatives.

(e) Keeping of Books. Keep, and cause each Material Subsidiary to keep, proper books of record and account, in which entries shall be made of all financial transactions and the assets and business of the Company and each Material Subsidiary in accordance with generally accepted accounting principles.

(f) Maintenance of Properties. Maintain and preserve, and cause each Material Subsidiary to maintain and preserve, all of its properties which are used or which are useful in the conduct of its business in good working order and condition, ordinary wear and tear excepted, it being understood that this covenant relates only to the good working

order and condition of such properties and shall not be construed as a covenant of the Company or any Material Subsidiary not to dispose of such properties by sale, lease, transfer or otherwise.

(g) Reporting Requirements. Furnish to the Bank the following: (i) as soon as practicable, and in any event within ten days after the Company knows or has reason to know of the occurrence of a Reimbursement Default which is continuing on the date of such statement, a statement of the chief financial officer (or in his absence, a principal financial officer) of the Company setting forth details of such Reimbursement Default and the action which the Company proposes to take with respect thereto; (ii) as soon as available and in any event within 15 days after filing of each of the Company's Reports on Form 8-K with the Securities and Exchange Commission, a copy of each such report; (iii) as soon as available and in any event within 30 days after filing of each of the Company's Reports on Form 10-Q with the Securities and Exchange Commission, a copy of each such report together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company stating (x) that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (iv) as soon as available and in any event within 30 days after filing of each of the Company's Annual Reports on Form 10-K with the Securities and Exchange Commission, a copy of each such report, together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (v) as soon as available and in any event within 20 days after any member of the Controlled Group (x) gives or is required to give notice to the PBGC of any "reportable event" (as defined in Section 4043 of ERISA) with respect to any Plan which might constitute grounds for the termination of such Plan under Title IV of ERISA, or knows

that the plan administrator of any Plan has given or is required to give notice of any such reportable event, a copy of the notice of such reportable event given or required to be given to the PBGC, provided that no such information need be given with respect to any reportable event for which the 30-day notice requirement of Section 4043(a) of ERISA has been waived, (y) receives notice of complete or partial withdrawal liability under Title IV of ERISA, a copy of such notice or (z) receives notice from the PBGC under the Title IV of ERISA of an intent to terminate or appoint a trustee to administer any Plan, a copy of such notice, (vi) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the Transaction Documents and Financing Documents and (vii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the Company as the Bank may from time to time reasonably request in writing.

(h) Maintenance of Equity. Maintain at all times consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied, of at least \$1.4 billion.

(i) Fixed Charge Ratio. Maintain at all times a Fixed Charge Ratio of at least 2 to 1. "Fixed Charge Ratio" shall mean at any time the ratio of (A) the sum of (x) the consolidated net income of the Company and its Consolidated Subsidiaries for the twelve month period ending with the last month for which the Company has prepared a consolidated income statement, which period shall in no event end earlier than the last day of the month two months prior to the time of the calculation of the Fixed Charge Ratio (the "Twelve Month Period") plus (y) all income taxes deducted in determining said consolidated net income plus (z) the sum of (i) all interest expense in respect of Indebtedness deducted in determining said consolidated net income, (ii) all interest expense in respect of Funded Indebtedness being incurred at the time of calculation of the Fixed Charge Ratio that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate and (iii) all interest expense in respect of Indebtedness other than Funded Indebtedness (I) incurred at any time subsequent to the Twelve Month Period outstanding at the time of the calculation of the Fixed Charge Ratio and (II) being incurred at the time of the calculation of the Fixed Charge Ratio, that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate, (iv) to the extent not covered under clauses

(i), (ii) or (iii) above, (I) rentals payable under Operating Lease Obligations during the Twelve Month Period and (II) with respect to Operating Lease Obligations entered into subsequent to the Twelve Month Period or being entered into at the time of calculation of the Fixed Charge Ratio, the rentals that would have been payable if such Operating Lease Obligations had been outstanding during the Twelve Month Period, provided that rentals payable under any Operating Lease Obligation shall not be included in the calculation of the Fixed Charge Ratio under this clause (iv) until the date that is nine months after the first day of the lease term of such Operating Lease Obligation (the aggregate interest expense and rental payments described in this clause (z) being referred to as the "Interest Expense") to (B) Interest Expense for such period.

SECTION 8. Negative Covenants. The Company agrees that, during the term of this Agreement it will not:

(a) Sales, Etc. of Assets. Sell, lease, transfer or otherwise dispose of (or pledge or otherwise encumber), in any one fiscal year in one or a series of transactions to one or more Persons, including any Subsidiary or Affiliate of the Company, assets with an aggregate value exceeding 10% of the value of the assets of the Company as shown on the consolidated balance sheet of the Company and its Consolidated Subsidiaries included in its audited financial statements for its most recent fiscal year, such assets to be valued on the same basis as that on which they were included in such consolidated financial statements, or, if such assets were not included in such consolidated financial statements, on the same basis as similar assets were valued for such consolidated financial statements, provided, however, that the Company may (i) pledge or encumber assets in connection with the sale of bonds issued under the Company Indenture, (ii) enter into sale and sale-back and sale and lease-back arrangements in connection with Unleased Interests and (iii) create or suffer to exist Excepted Encumbrances as defined in the Company Indenture.

(b) Mergers, Etc. Merge with or into or consolidate with or into any other corporation or entity, or permit any Subsidiary to do so unless (i) immediately after giving effect thereto, no event shall occur and be continuing which constitutes a Reimbursement Default, (ii) the consolidation or merger shall not materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents and (iii) in the case of any merger or consolidation to which the Company is a party, the corporation

formed by such consolidation or into which the Company shall be merged shall assume the Company's obligations under this Agreement in a writing satisfactory in form and substance to the Bank.

(c) Compliance with ERISA. (i) Enter into any prohibited transaction (as defined in Section 4975 of the Internal Revenue Code of 1954, as amended, and in ERISA) involving any Plan which results in any liability of the Company to any Person which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company or (ii) allow or suffer to exist any other event or condition known to the Company which results in any liability of the Company to the PBGC which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company. For purposes of this Section 8(c), "liability" shall not include the contingent liability described in Sections 4201 and 4062 of ERISA or termination insurance premiums payable under Section 4007 of ERISA.

(d) Assignment of Transaction Documents or Financing Documents. After the Date of Issuance, enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents, without first obtaining the express prior written consent of the Bank thereto.

SECTION 9. Reimbursement Events of Default. The following events shall be Reimbursement Events of Default hereunder unless waived by the Bank pursuant to Section 10 hereof:

(i) the Company shall fail to pay when due any amount payable under Section 2 hereunder; or

(ii) the Company shall fail to observe or perform any covenant or agreement contained in this Agreement (other than those covered by clause (i) above or Sections 7(d) and 18 hereof) for 30 days after written notice thereof has been given to the Company by the Bank; or

(iii) any representation, warranty, certification or statement made by the Company in this Agreement or in any certificate, financial statement or other document delivered pursuant to this Agreement shall prove to have been incorrect in any material respect when made; or

(iv) any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) the Company shall (x) fail to make any payment, equal to or exceeding \$5,000,000 of any Outstanding Debt, or to make any payment, equal to or exceeding \$5,000,000, of any interest or premium thereon, when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument relating to the Outstanding Debt, or (y) fail to perform or observe any other term, covenant or condition on its part to be performed or observed under any agreement or instrument relating to any Outstanding Debt when required to be performed or observed, and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure to perform or observe is to accelerate, or to permit the acceleration of, the maturity of any Outstanding Debt, the unpaid principal amount of which then equals or exceeds \$5,000,000; or

(vi) the Company shall (A) apply for or consent to the appointment of a receiver, trustee, liquidator or custodian or the like of itself or of its property, (B) admit in writing its inability to pay its debts generally as they become due, (C) make a general assignment for the benefit of creditors, (D) be adjudicated a bankrupt or insolvent, or (E) commence a voluntary case under the Federal bankruptcy laws of the United States of America or file a voluntary petition or answer seeking reorganization, an arrangement with creditors or any order for relief or seeking to take advantage of any insolvency law or file an answer admitting the material allegations of a petition filed against it in any bankruptcy, reorganization or insolvency proceeding; or corporate action shall be taken by it for the purpose of effecting any of the foregoing, or if without the application, approval or consent

of the Company, a proceeding shall be instituted in any court of competent jurisdiction, seeking in respect of the Company an adjudication in bankruptcy, reorganization, dissolution, winding up, liquidation, a composition or arrangement with creditors, a readjustment of debts, the appointment of a trustee, receiver, liquidator or custodian or the like of the Company or of all or any substantial part of its assets, or other like relief in respect thereof under any bankruptcy or insolvency law, and, if such proceeding is being contested by the Company in good faith, the same shall (i) result in the entry of an order for relief of any such adjudication or appointment or (ii) continue undismissed, or pending and unstayed, for any period of seventy-five (75) consecutive days; or

(vii) any judgment or order for the payment of money exceeding any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and either (i) enforcement proceedings shall have been commenced by any creditor upon such judgment or order or (ii) there shall be any period of ten consecutive days during which a stay of enforcement of such judgment or order, by reason of a pending appeal or otherwise, shall not be in effect; or

(viii) the Company or any member of the Controlled Group shall fail to pay when due an amount or amounts aggregating in excess of \$5,000,000 which it shall have become liable to pay to the PBGC or to a Plan under Title IV of ERISA; or notice of intent to terminate a Plan or Plans having aggregate Unfunded Vested Liabilities in excess of \$10,000,000 (collectively a "Material Plan") shall be filed under Title IV of ERISA by the Company, any member of the Controlled Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate or to cause a trustee to be appointed to administer any Material Plan; or a proceeding shall be instituted by a fiduciary of any Material Plan against the Company or any member of the Controlled Group to enforce Section 515 of ERISA in which the amount in controversy exceeds \$1,000,000 and such proceeding shall not have been dismissed within 30 days thereafter; or a condition shall exist by reason of which the PBGC would be entitled under

Title IV of ERISA to obtain a decree adjudicating that any Material Plan must be terminated; or

(ix) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(x) any event specified in Sections 15 (vii), (viii) or (x) of the Facility Lease shall occur; or

(xi) the Company shall fail to make, or cause to be made, any payment specified in Section 15 (i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

If an Event of Default occurs and is continuing, the Bank may, in its sole discretion by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein.

SECTION 10. Amendments and Waivers. No amendment or waiver of any provision of this Agreement, nor consent to any departure by the Company therefrom nor any consent to the assignment of the Company's obligations under the Transaction Documents or the Financing Documents shall in any event be effective unless the same shall be in writing and signed by the Bank. Any such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given.

SECTION 11. Notices. All notices, requests and other communications to any party hereunder shall be in writing (including telex or similar writing) and shall be given to such party, addressed to it, at its address or telex number set forth below or such other address or telex number as such party may hereafter specify for the purpose by notice to the other party. Each such notice, request or communication shall be effective (i) if given by telex, when such telex is transmitted to the telex number specified below and the appropriate answerback is received, (ii) if given by mail upon receipt but not later than 10 days after such communication is deposited in the mails with first class postage prepaid, addressed as aforesaid or (iii) if given by any other means, when delivered at the address specified below.

Party
Arizona Public Service
Company

Address
Street Address:
411 North Central Avenue
Phoenix, Arizona 85004

Mailing Address:
P.O. Box 53999
Phoenix, Arizona 85072-3999
Attention: Treasurer
Telex: TWX165232
Answerback: APS PHNX
Facsimile Transmission:
(602) 250-2061

Morgan Guaranty Trust
Company of New York

150 William Street
17th Floor
New York, New York 10015
Attn: Letter of Credit
Department
(Copy to
Utilities Department)
Telex: 420230
Answerback: MGT UI
or
Telex: 232194
Answerback: MGT UR
Facsimile Transmission:
(212) 344-9454

SECTION 12. No Waiver; Remedies. No failure on the part of the Bank to exercise, and no delay in exercising, any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise of any right hereunder preclude any other further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

SECTION 13. Waiver of Right of Setoff. The Bank hereby waives any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by the Bank to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up,

reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "bankruptcy events"), against any and all of the obligations of the Company now or hereafter existing in respect of the reimbursement obligation of the Company set forth in Section 2(a) hereof, provided any such waiver shall be deemed ineffective as and to the extent that the Bank receives, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience, (which counsel shall be mutually satisfactory to the Bank and the Owner Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section.

SECTION 14. Sales of Participations. The Bank may grant participations under this Agreement and the Letters of Credit (each person to which a participation is granted being called a "Participant") and in such event the Bank will in its own name and as agent for any Participant, enforce all rights and interests of any Participant under this Agreement, and accept all performances required of the Company under this Agreement, provided that (i) the Bank shall not agree to a substitution or replacement of a Participant or a change in the proportionate amount of any Participant's participation after the Date of Issuance unless the Bank shall have received the Company's prior written consent thereto, which consent shall not be unreasonably withheld and (ii) in the event that a claim for compensation is made pursuant to Section 2(c) on behalf of a Participant, the Company shall have the right, with the assistance of the Bank, to seek a substitute participant or participants, satisfactory to the Bank, to assume the participation of such Participant.

SECTION 15. Continuing Obligation. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date or (ii) the date upon which all amounts due and owing to the Bank hereunder shall have been paid in full and shall (a) be binding upon the Company

and its successors and assigns and (b) inure to the benefit of and be enforceable by the Bank and its successors, transferees and assigns, provided, however, that the Company may not assign all or any part of this Agreement without the prior written consent of the Bank.

SECTION 16. Extension of Letter of Credit. At least 90 but not more than 180 days before the fifth anniversary of the Date of Issuance, the Company may request the Bank in writing to extend for not less than three years, nor more than eight years, the Termination Date of the Letter of Credit, specifying the terms and conditions, including fees, to be applicable to such extension. No later than 30 days from the date on which the Bank shall have received notice from the Company pursuant to the preceding sentence, the Bank shall notify the Company of its consent or nonconsent to such extension request, and if the Bank shall give no such notice, the Bank shall be deemed not to have consented to such extension request. The Bank's consent shall be conditional upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to the Bank and its counsel incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement between the Company and the Bank.

SECTION 17. Limited Liability of the Bank. The Company assumes all risks of the acts or omissions of the Equity Participant with respect to its use of the Letter of Credit. Neither the Bank nor any of its officers or directors shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or for any acts or omissions of the Equity Participant in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement(s) thereon, even if such documents should in fact prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except only that the Company shall have a claim against the Bank, and the Bank shall be liable to the Company to the extent, but only to the extent, of any direct, as opposed to consequential, damages suffered by the Company which the Company proves were caused by (i) the Bank's willful misconduct or gross negligence in determining whether documents presented under the Letter of Credit comply with the terms thereof or (ii) the Bank's willful failure to pay under the Letter of Credit after the

presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. In furtherance and not in limitation of the foregoing, the Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

SECTION 18. Costs, Expenses and Taxes. The Company agrees to pay not later than 30 days after demand therefor all reasonable costs and expenses in connection with the preparation, execution, delivery, filing and administration of this Agreement and any other documents which may be delivered in connection with this Agreement, including, without limitation, the reasonable fees and out-of-pocket expenses of counsel for the Bank with respect thereto and with respect to advising the Bank as to its rights and responsibilities under this Agreement or any waiver or amendment of, or the enforcement of, this Agreement and such other documents which may be delivered in connection with this Agreement. In addition, the Company shall pay any and all stamp and other taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents and agrees to save the Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, provided that the Bank agrees promptly to notify the Company of any such taxes and fees which are incurred by the Bank.

SECTION 19. Indemnification. The Company hereby agrees to indemnify and hold harmless the Bank from and against any and all claims, damages, losses, liabilities, costs or expenses whatsoever which the Bank may incur (or which may be claimed against the Bank by any person or entity whatsoever) (i) by reason of any inaccuracy in any material respect, or untrue statement or alleged untrue statement of any material fact contained or incorporated by reference in any offering document distributed by or on behalf of the Company in connection with obtaining purchasers of the Company's undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station, or in any supplement or amendment to either thereof, or the omission or alleged omission to state therein a material fact necessary to make such statements, in the light of the circumstances under which they are or were made, not misleading; (ii) by reason of or in connection with

the execution, delivery and performance of the Transaction Documents and Financing Documents; or (iii) by reason of or in connection with the execution and delivery or transfer of, or payment or failure to make lawful payment under, the Letter of Credit; provided that the Company shall not be required to indemnify the Bank for any claims, damages, losses, liabilities, costs or expenses to the extent, but only to the extent, caused by the willful misconduct or gross negligence of the Bank in determining whether a draft or certificate presented under the Letter of Credit complied with the terms of the Letter of Credit or the Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. Nothing in this Section 19 is intended to limit the Company's reimbursement obligation contained in paragraph (a) of Section 2 hereof. Without prejudice to the survival of any other obligation of the Company hereunder, the indemnitees and obligations of the Company contained in this Section 19 shall survive the payment in full of amounts payable under Section 2 and the termination of the Letter of Credit.

SECTION 20. Severability. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

SECTION 21. Governing Law. This Agreement shall be governed by, and construed and interpreted in accordance with, the laws of the State of New York.

SECTION 22. Headings. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By 

Title:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK

By 

Title: Vice President

IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. S-1001

August 18, 1986

Security Pacific Capital
Leasing Corporation
Four Embarcadero Center
Suite 1200
San Francisco, California 94111

Attn: Chief Counsel
Manager - Lease Investments
Manager - Lease Services

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "Company"), in your favor, our Irrevocable Transferable Letter of Credit No. S-1001 (the "Letter of Credit"), in an amount not to exceed \$45,259,626.31 (the "Maximum Credit Amount"), effective immediately and expiring at 5:00 p.m. (New York time) on the Termination Date. Capitalized terms used herein and in Schedules II and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "Facility Lease") between the Company and the First National Bank of Boston, as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "Date of Drawing") in the Table of Maximum Drawing Amounts attached hereto as Schedule II as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next paragraph, are hereinafter referred to collectively as the "Maximum Drawing Amounts" and

individually as the "Maximum Drawing Amount". A drawing in respect of a payment hereunder honored by us shall not exceed the lesser of the Maximum Drawing Amount applicable on the Date of Drawing and the Maximum Credit Amount.

The Maximum Drawing Amounts shall be modified from time to time as follows:

(a) upon payment by the Bank of each drawing under the Letter of Credit, the Maximum Drawing Amounts applicable to each Date of Drawing subsequent to such payment shall be automatically reduced by an amount equal to the amount of the drawing so paid and shall not be reinstated; and

(b) if adjustments are made to Modified Special Casualty Values, corresponding adjustments shall be made to the Maximum Drawing Amounts shown in Schedule II, (as theretofore reduced pursuant to clause (a) above), provided that if any such adjustment of Modified Special Casualty Values would cause the Maximum Drawing Amount for any period to exceed the Maximum Credit Amount, the Maximum Credit Amount shall apply for such period and provided further that adjustments pursuant to this clause (b) shall be effective automatically upon receipt by us of a notice from you in the form of Exhibit 1 hereto.

Upon surrender of this Letter of Credit together with a notice in the form of Exhibit 1 hereto, we will promptly issue an irrevocable transferable letter of credit containing a revised Schedule II reflecting the adjustments contained in such notice and in all other respects identical to this Letter of Credit.

Funds under this Letter of Credit are available to you against presentation on or prior to the Termination Date of (a) your draft in the form of Exhibit 2 attached hereto and (b) a completed certificate signed by you in the form of Exhibit 3 attached hereto. Such draft and certificate shall be dated the date of presentation and shall be made at our office located at 23 Wall Street, New York New York 10015, Attention: Letter of Credit Department (or at any other office in the City and State of New York which may be designated by us by written notice (given in the manner set forth in the next paragraph) delivered to you at least 15 days prior to the applicable Date of Drawing). If we receive such draft and certificate at such office, all in strict conformity with the terms and conditions of this Letter of Credit, prior to 10:00 a.m. (New York time) on any Business Day, we will honor the draft on the same Business Day. If we receive such draft and certificate at such office, all in strict conformity with the terms and conditions of this Letter of Credit, on or after 10:00 a.m. (New York

time) on any Business Day, we will honor the draft on the next Business Day. If requested by you, payment under this Letter of Credit may be made by wire transfer of federal funds to your account with any bank located in the United States of America or by deposit of immediately available funds into a designated account that you maintain with us.

Notwithstanding any other provision of this Letter of Credit, we shall have the right, upon the occurrence of any of the events listed in Schedule III hereto, to terminate this Letter of Credit by delivering to you a written notice indicating the date of such termination (the "Date of Early Termination"), provided that on or before the Date of Early Termination you will have the right to draw once an amount not in excess of the Maximum Drawing Amount in accordance with the procedures described herein. The written notice referred to in the preceding sentence shall be given by telex or facsimile transmission addressed to you at Security Pacific Capital Leasing Corporation, Four Embarcadero Center, Suite 1200, San Francisco, California 94111, Telex: 9103722123, Attention: Chief Counsel, Manager - Lease Investments, Manager - Lease Services, Answerback: SPLC SFO (or to such other address or telex number designated by you by written notice delivered to us at least 15 days prior to the notice of early termination) and shall be effective upon receipt of the appropriate answerback or confirmation of the facsimile transmission. We will also forward a copy of such notice by overnight delivery service to the address set forth above. The Date of Early Termination specified in such written notice shall be:

(a) in the case of events specified in paragraphs A and F of Schedule III, not earlier than ten days after such notice is given, and

(b) in the case of all other events specified in Schedule III, not earlier than 30 days after such notice is given.

Except as set forth below, this Letter of Credit shall be governed by the Uniform Customs and Practice for Documentary Credits (revision effective October 1, 1984) International Chamber of Commerce Publication No. 400, and, as to matters not covered therein, be governed by the laws of the State of New York, including without limitation the Uniform Commercial Code as in effect in such State. Communications with respect to this Letter of Credit shall be in writing and shall be addressed to us at 23 Wall Street, New York, New York 10015, Attention: Letter of Credit Department (with a copy to Utilities Department) and shall specifically refer to the number of this Letter of Credit.

Notwithstanding Article 54 of the Uniform Customs and Practice for Documentary Credits referred to above, this Letter of Credit may be transferred and assigned in its entirety more than once, but in each case only to the successor Owner Participant under the Trust Agreement dated as of August 1, 1986 between yourself and the First National Bank of Boston. Upon receipt by us at the address for presentation of documents set forth above of a copy of the instrument effecting such transfer and assignment, signed by the transferor and by the transferee, in the form of Exhibit 4 hereto (which shall be conclusive evidence of such assignee's authority without any inquiry by us into the terms of the Trust Agreement) then, in such case, we will, upon surrender of this Letter of Credit, issue an irrevocable transferable letter of credit in the name of the transferee and providing for notices to be sent to the transferee at the address set forth therein and in all other respects identical to this Letter of Credit and the transferee, instead of the transferor, shall, without necessity of further act, be entitled to all the benefits of, and rights under, this Letter of Credit in the transferor's place.

By your acceptance of this Letter of Credit, you hereby agree, and we hereby confirm our agreement, to the terms and conditions of Section 13 of the Reimbursement Agreement.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein, except only Schedules I, II and III and Exhibits 1, 2, 3 and 4 hereto and the notices referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except as set forth above.

Very truly yours,

MORGAN GUARANTY TRUST
COMPANY OF NEW YORK

By /s/ David A. Behnke
Title: Vice President

Morgan Guaranty Trust
Company of New York
23 Wall Street
New York, New York 10015
Attention: Letter of Credit Department

Dear Sirs:

Reference is made to that certain irrevocable transferable Letter of Credit bearing Letter of Credit No. _____ dated [Date of Issuance], which has been established by you in favor of [name of Equity Participant] (the "Equity Participant").

The undersigned, a duly authorized representative of the Equity Participant, hereby certifies that Modified Special Casualty Values have been adjusted and the amounts shown on Schedule II to the Letter of Credit should be modified, in accordance with the terms of clauses (a) and (b) of the third paragraph of the Letter of Credit, to the amounts shown in Appendix A hereto.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit with the revised Schedule II attached and in all other respects identical to the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

[Name of Equity Participant]

[Name and Title of Authorized
Representative of Equity Participant]

EXHIBIT 2

[Place]

[Date] 19

ON [Business Day of presentation if presented before 10:00 a.m.
(New York time); next Business Day if presented after 10:00 a.m.]

PAY TO

[Name of beneficiary]

U.S. \$[not to exceed Maximum
Drawing Amount]
DOLLARS,

FOR VALUE RECEIVED AND CHARGE TO ACCOUNT OF LETTER OF

CREDIT NO.

OF

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

[Name and Address of
Equity Participant]

By _____
[Authorized Representative]

CERTIFICATE

The undersigned, a duly authorized representative of [name of Equity Participant] (the "Equity Participant"), as beneficiary under that certain irrevocable transferable Letter of Credit No. _____ dated [the Date of Issuance], established by Morgan Guaranty Trust Company of New York (the "Bank") and issued pursuant to that certain Reimbursement Agreement dated as of August 1, 1986 (the "Reimbursement Agreement") between Arizona Public Service Company (the "Company") and the Bank, hereby certifies as follows:

1. An Event of Default under the Facility Lease has occurred and is continuing.

2. The amount of the accompanying draft does not exceed the Maximum Drawing Amount available under the Letter of Credit on the date hereof, as determined in accordance with the terms of the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed this Certificate as of _____, 19 .

[Name of Equity Participant]

[Name and title of authorized
representative signing certificate]

Morgan Guaranty Trust
Company of New York
23 Wall Street
New York, NY 10005

Dear Sirs:

Reference is made to the certain irrevocable transferable Letter of Credit bearing Letter of Credit No. dated [Date of Issuance], which has been established by you in favor of [name of Equity Participant (the "Transferor")].

The Transferor has transferred and assigned (and hereby confirms to you said transfer and assignment) all of its rights in and under said Letter of Credit to [name of Transferee (the "Transferee")] and confirms that the Transferor no longer has any rights under or interest in said Letter Credit.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit in the name of the Transferee and providing for notices to be sent to the Transferee at the address set forth below and in all other respects identical to the Letter of Credit.

Transferee hereby certifies that it is a duly authorized transferee under the terms of said Letter of Credit and is accordingly entitled, upon presentation of the drafts and certificates called for therein, to receive payment thereunder. Notices under the Letter of Credit should be sent to us as follows: [Name], [Address], [Telex Number], Attention: , [Answerback].

[Name of Transferor]

[Name and Title of Authorized
Representative of Transferor]

[Name of Transferee]

[Name and Title of Authorized
Representative of Transferee]

Schedule I

The following terms shall have the following meanings for purposes of the Letter of Credit and the Schedules and Exhibits thereto. Terms defined in the Letter of Credit shall have the meanings given to them therein. Terms defined by reference to the Facility Lease shall have the meanings assigned to them therein from time to time.

"Aggregate Operating Lease Obligations" of any Person means all Operating Lease Obligations under operating leases which are entered into by such Person in substantially contemporaneous transactions.

"Applicable Law" has the meaning assigned to it in the Facility Lease.

"Business Day" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois and the State of California are authorized by law to close.

"Controlled Group" means all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Company, are treated as a single employer under Section 414(b) or 414(c) of Code.

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

"Governmental Action" has the meaning assigned to it in the Facility Lease.

"Modified Special Casualty Value" has the meaning assigned to it in the Facility Lease.

"Operating Lease Obligations" of any Person means all obligations of such Person as lessee under each operating lease of all or a portion of any Unleased Interests.

"Outstanding Debt" of any Person means at any date, without duplication, (i) all obligations of such Person for borrowed money, (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business, (iv) all obligations of such Person as lessee under capital leases, (v) all Aggregate Operating Lease Obligations of such Person, (vi) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, (vii) all Outstanding Debt of others secured by a Lien on any asset of such Person, whether or not such Outstanding Debt is assumed by such Person, and (viii) all obligations, contingent or otherwise, of such Person directly or indirectly guaranteeing any Outstanding Debt of any other Person or in any manner providing for the payment of any Outstanding Debt of any other Person or otherwise protecting the holder of such Outstanding Debt against loss (whether by agreement to keep-well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), excluding, however, from this clause (viii) endorsements for collection or deposit in the ordinary course of business.

"PBGC" means the Pension Benefit Guaranty Corporation and any entity succeeding to any or all of its functions under ERISA.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" means at any time an employee pension benefit plan which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Code and is either (i) maintained by a member of the Controlled Group for employees of a member of the Controlled Group or (ii) maintained pursuant to a collective bargaining agreement or any other arrangement under which more than one employer makes contributions and to which a member of the

Controlled Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions.

"Reimbursement Agreement" means the Reimbursement Agreement, dated as of August 1, 1986 between the Company and the Bank as the same may from time to time be amended, supplemented or modified.

"Termination Date" means the earlier of (i) the date on which the Bank pays a drawing under the Letter of Credit for the Maximum Drawing Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Bank pays such drawing, (iv) the date on which the Company pays the amounts due under Section 9(c) of the Facility Lease, (v) the date on which the Company pays the amounts due under Section 9(d) of the Facility Lease or (vi) either (x) the fifth anniversary of the Date of Issuance of the Letter of Credit or (y) if a draft and certificate, all in strict conformity with the terms and conditions of the Letter of Credit, are presented after 10:00 a.m. but prior to 5:00 p.m. (New York time) on the fifth anniversary of the Date of Issuance of the Letter of Credit, the Business Day following such fifth anniversary.

"Transaction Documents" means the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, the Real Property Interest and the Notes, each as defined in the Facility Lease.

"Unfunded Vested Liabilities" means, with respect to any Plan at any time, the amount (if any) by which (i) the present value of all vested nonforfeitable benefits under such Plan exceeds (ii) the fair market value of all Plan assets allocable to such benefits, all determined as of the then most recent valuation date for such Plan, but only to the extent that such excess represents a potential liability of a member of the Controlled Group to the PBGC or the Plan under Title IV of ERISA.

"Unit 2" has the meaning assigned to it in the Facility Lease.

"Unit 3" means the 1270 megawatt unit, commonly known as Unit 3, at the Palo Verde Nuclear Generating Station, together with all capital improvements thereto.

"Unleased Interests" means any real or personal or mixed property interest of any Person in that portion of Unit 2 and Unit 3 of the Palo Verde Nuclear Generating Station which is not subject to an operating lease immediately after the Letter of Credit has been issued by the Bank.

Schedule II

Table of Maximum Drawing Amounts

<u>Applicable Period</u>	<u>Maximum Drawing Amount</u>
From August 18, 1986 to and including July 10, 1987	\$36,180,870
From July 11, 1987 to and including January 10, 1988	\$40,118,954
From January 11, 1988 to and including July 10, 1988	\$43,594,080
From July 11, 1988 to and including January 10, 1989	\$46,655,106
From January 11, 1989 to and including July 10, 1989	\$49,296,303
From July 11, 1989 to and including January 10, 1990	\$51,570,167
From January 11, 1990 to and including July 10, 1990	\$53,456,627
From July 11, 1990 to and including January 10, 1991	\$54,925,474
From January 11, 1991 to and including July 10, 1991	\$55,942,558
From July 11, 1986 to and including August 18, 1991	\$56,472,090

Schedule III

The Bank shall have the right upon the occurrence of any of the events listed below to terminate the Letter of Credit in accordance with the terms of the Letter of Credit:

(A) the Company shall fail to pay when due any amount payable under Section 2 of the Reimbursement Agreement;

(B) the Company shall fail to observe or perform any covenant or agreement contained in the Reimbursement Agreement (other than those covered by clause (i) above or Sections 7(d) and 18 of the Reimbursement Agreement) for 30 days after written notice thereof has been given to the Company by the Bank;

(C) any representation, warranty, certification or statement made by the Company in the Reimbursement Agreement or in any certificate, financial statement or other document delivered pursuant to the Reimbursement Agreement shall prove to have been incorrect in any material respect when made;

(D) any material provision of the Reimbursement Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under the Reimbursement Agreement;

(E) the Company shall (x) fail to make any payment, equal to or exceeding \$5,000,000 of any Outstanding Debt, or to make any payment, equal to or exceeding \$5,000,000, of any interest or premium thereon, when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument relating to the Outstanding Debt, or (y) fail to perform or observe any other term, covenant or condition on its part to be performed or observed under any agreement or instrument relating to any Outstanding Debt when required to be performed or observed, and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure to perform or observe is to accelerate, or to permit the acceleration of, the maturity of any Outstanding Debt, the unpaid principal amount of which then equals or exceeds \$5,000,000; or

(F) the Company shall (i) apply for or consent to the appointment of a receiver, trustee, liquidator or custodian or the like of itself or of its property, (ii) admit in writing its inability to pay its debts generally as they become due, (iii) make a general assignment for the benefit of creditors, (iv) be adjudicated a bankrupt or insolvent, or (v) commence a voluntary case under the Federal bankruptcy laws of the United States of America or file a voluntary petition or answer seeking reorganization, an arrangement with creditors or any order for relief or seeking to take advantage of any insolvency law or file an answer admitting the material allegations of a petition filed against it in any bankruptcy, reorganization or insolvency proceeding; or corporate action shall be taken by it for the purpose of effecting any of the foregoing, or if without the application, approval or consent of the Company, a proceeding shall be instituted in any court of competent jurisdiction, seeking in respect of the Company an adjudication in bankruptcy, reorganization, dissolution, winding up, liquidation, a composition or arrangement with creditors, a readjustment of debts, the appointment of a trustee, receiver, liquidator or custodian or the like of

the Company or of all or any substantial part of its assets, or other like relief in respect thereof under any bankruptcy or insolvency law, and, if such proceeding is being contested by the Company in good faith, the same shall (a) result in the entry of an order for relief of any such adjudication or appointment or (b) continue undismissed, or pending and unstayed, for any period of seventy-five (75) consecutive days; or

(G) any judgment or order for the payment of money exceeding any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and either (i) enforcement proceedings shall have been commenced by any creditor upon such judgment or order or (ii) there shall be any period of ten consecutive days during which a stay of enforcement of such judgment or order, by reason of a pending appeal or otherwise, shall not be in effect; or

(H) the Company or any member of the Controlled Group shall fail to pay when due an amount or amounts aggregating in excess of \$5,000,000 which it shall have become liable to pay to the PBGC or to a Plan under Title IV of ERISA; or notice of intent to terminate a Plan or Plans having aggregate Unfunded Vested Liabilities in excess of \$10,000,000 (collectively a "Material Plan") shall be filed under Title IV of ERISA by the Company, any member of the Controlled Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate or to cause a trustee to be appointed to administer any Material Plan; or a proceeding shall be instituted by a fiduciary of any Material Plan against the Company or any member of the Controlled Group to enforce Section 515 of ERISA in which the amount in controversy exceeds \$1,000,000 and such proceeding shall not have been dismissed within 30 days thereafter; or a condition shall exist by reason of which the PBGC would be entitled under Title IV of ERISA to obtain a decree adjudicating that any Material Plan must be terminated; or

(I) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by

the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(J) any event specified in Sections 15 (vii), (viii) or (x) of the Facility Lease shall occur; or

(K) the Company shall fail to make, or cause to be made, any payment referred to in Section 15 (i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

LAW OFFICES
SNELL & WILMER
3100 VALLEY BANK CENTER
PHOENIX, ARIZONA 85073
(602) 257-7211

August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Re: Arizona Public Service Company

Gentlemen:

We are members of the Arizona Bar and are general counsel to Arizona Public Service Company, an Arizona corporation (the "Company"). In that capacity, we are familiar with the matters relating to the preparation, execution and delivery of a Reimbursement Agreement (the "Reimbursement Agreement"), dated as of August 1, 1986, between the Company and Morgan Guaranty Trust Company of New York (the "Bank"). All capitalized terms used herein and defined in the Reimbursement Agreement are used herein as therein defined.

In connection with the foregoing, we have examined, among other things, the following:

- (1) fully executed counterparts of the Reimbursement Agreement;
- (2) the fully executed Letter of Credit;
- (3) a recently certified copy of the Articles of Incorporation of the Company and all amendments thereto (the "Charter");
- (4) a recently certified copy of the Bylaws of the Company as now in effect (the "Bylaws");
- (5) a certificate of the Arizona Corporation Commission, dated August 11, 1986, attesting to the continued corporate existence and the good standing of the Company in that State; and certificates, telegrams, telexes (or have received telephone confirmations) from the State of New Mexico, dated as of a recent date, attesting to the qualification to do business and the good standing of the Company in that State; and

Morgan Guaranty Trust Company
of New York
August 18, 1986
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(6) the Company's corporate proceedings and the proceedings before the Arizona Corporation Commission relating to the Reimbursement Agreement and related matters.

We have also examined the originals, or copies certified to our satisfaction, of the agreements, instruments and documents which affect or purport to affect the obligations of the Company under the Reimbursement Agreement and (i) such other corporate records of the Company, certificates of public officials and of officers of the Company, and (ii) such other agreements, instruments and documents, as we have deemed necessary as a basis for the opinions hereinafter expressed. As to questions of fact material to such opinions, we have, when relevant facts were not independently established by us, relied upon certificates of the Company or its officers or of public officials. We have assumed the due execution and delivery, pursuant to due authorization, of the Reimbursement Agreement by the Bank.

Based upon the foregoing and upon such other investigation as we have deemed necessary, we are of the opinion that, insofar as the laws of the State of Arizona are concerned:

(1) The execution, delivery and performance by the Company of the Reimbursement Agreement are within the Company's corporate power, have been duly authorized by all necessary corporate action, and do not contravene (i) the Charter or the Bylaws, or (ii) any law, rule or regulation or (iii) to the best of our knowledge, any contractual or legal restriction (including, but not limited to, the Existing Mortgage) binding on or affecting the Company, and do not result in or require the creation of any lien, security interest or other charge or encumbrance (other than pursuant to the Reimbursement Agreement) upon or with respect to any of its properties. The Reimbursement Agreement has been duly executed and delivered on behalf of the Company.

(2) The Arizona Corporation Commission has duly issued an order (Decision No. 55120) authorizing the Company to enter into the Reimbursement Agreement and to take all actions contemplated thereby or in connection therewith, and such order remains in full force and effect in the form issued. No other authorization, approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due

Morgan Guaranty Trust Company
of New York
August 18, 1986
Page 3

execution, delivery and performance by the Company of the Reimbursement Agreement.

(3) The Reimbursement Agreement is the legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms; provided, however, that we express no opinion with respect to the enforceability of Sections 5 and 12 of the Reimbursement Agreement.

(4) There is no pending action or proceeding before any court, governmental agency or arbitrator against or directly involving the Company or any of its subsidiaries and, to the best of our knowledge, there is no pending or threatened action or proceeding affecting the Company or any of its subsidiaries before any court, governmental agency or arbitrator (A) in which any question is raised as to the validity of the Reimbursement Agreement, or (B) (except as set forth in (i) the Company's Report on Form 10-K for the fiscal year ended December 31, 1985 in Item 1 thereof under "Rates-State," "Environmental Requirements," "Generating Fuel," "Water Supply" and "Indian Matters" or in Item 2 thereof, (ii) the Company's Report on Form 10-Q for the fiscal quarter ended March 31, 1986 under "Environmental Requirements," "Retail Rates," and "Palo Verde Nuclear Generating Station," and (iii) the Company's Report on Form 10-Q for the fiscal quarter ended June 30, 1986 under "Water Supply," "Retail Rates," and "Palo Verde Nuclear Generating Station") in which there is any material likelihood of an outcome which may materially and adversely affect the ability of the Company to perform its obligations under the Reimbursement Agreement. There has been no determination (interim or final) in any action or proceedings so disclosed which determination may materially adversely affect the ability of the Company to perform its obligations under the Reimbursement Agreement.

The opinions set forth above are subject to the following qualifications:

(a) The enforceability of the Company's obligations under the Reimbursement Agreement is subject to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors' rights generally.

(b) The enforceability of the Company's obligations under the Reimbursement Agreement may be subject to

Morgan Guaranty Trust Company
of New York
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general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

(c) We are not experts in the laws of the State of New York. In giving the opinion set forth in paragraph 4 above, we have relied, insofar as the laws of the State of New York are concerned, on the opinion of Mudge Rose Guthrie Alexander and Ferdon delivered to you pursuant to Section 3(b)(ii) of the Reimbursement Agreement.

We acknowledge that we are delivering to you, and you are entitled to rely upon, a separate opinion letter, dated the date hereof, concerning the enforceability of the Transaction Documents and related matters.

Very truly yours,

Snell & Wilmer

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August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Re: Arizona Public Service Company:

Gentlemen:

We have acted as general counsel for Arizona Public Service Company, an Arizona corporation ("APS"), in connection with the transactions contemplated by the Participation Agreement, dated as of August 1, 1986 (the "Participation Agreement"), among the Equity Participant listed on the attached Schedule, Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants under the Bank Agency Agreement, The First National Bank of Boston, a national banking association ("FNB"), individually and as Owner Trustee, PVNGS Funding Corp., Inc., a Delaware corporation, Chemical Bank, a New York banking corporation, in its individual capacity and as Indenture Trustee, and APS. We are also familiar with the matters relating to the preparation, execution and delivery of a Reimbursement Agreement (the "Reimbursement Agreement"), dated as of August 1, 1986, between APS and Morgan Guaranty Trust Company (the "Bank"). All capitalized terms used herein and not otherwise defined herein shall have the meanings set forth in Appendix A to the Participation Agreement. This opinion is being delivered pursuant to Section 11(a)(20) of the Participation Agreement and Section 3(b)(i) of the Reimbursement Agreement.

As such counsel we have examined originals or copies, certified or otherwise identified to our satisfaction, of such corporate records, agreements and other instruments, certificates, orders, opinions, correspondence with public officials, certificates of officers and representatives of APS, and other documents, as we have deemed necessary or advisable for the purposes of rendering the opinions set forth herein.

In rendering our opinions, we have also reviewed the Special Order of Exemption, issued December 26, 1985, by

the Arizona Department of Real Estate with respect to PVNGS, together with two (2) Snell & Wilmer petition letters to the Arizona Department of Real Estate, dated December 19, 1985 and December 23, 1985.

In rendering our opinions, we have relied as to certain factual matters on the documents we have examined, on certificates of public officials, and on the Certificate attached as Exhibit A, and we have assumed:

1. Each party to each Transaction Document, other than APS, is duly organized and validly existing in good standing under the laws of the jurisdiction of its organization, is duly registered, licensed or authorized to transact business in each other jurisdiction in which such registration, licensing or authorization is required, and has the power and the authority to enter into and to perform its obligations under each Transaction Document to which it is a party.

2. The execution, delivery and performance by each party to each Transaction Document, other than APS, have been duly authorized by all necessary action by such party and do not require the consent or approval of any of the stockholders of such party or, if required, such consent or approval has been obtained. Each Transaction Document has been duly executed and delivered by each party thereto, other than APS, and constitutes the legal, valid and binding obligation of such party, enforceable against such party in accordance with its terms.

3. The trusts of which the Owner Trustee and the Indenture Trustee are the Owner Trustee and the Indenture Trustee, respectively, were duly formed and are validly existing under the laws of the jurisdiction governing such trusts. Each of the Owner Trustee and the Indenture Trustee has the power and authority under the trust agreement for its respective trust to enter into and perform its obligations under each Transaction Document to which it is a party.

4. The Indenture Trustee is licensed, chartered, or regulated by the Federal Deposit Insurance Corporation or the Comptroller of the Currency.

5. The execution, delivery and performance by the Owner Trustee and the Indenture Trustee of each Transaction Document to which it is a party are authorized by the trust

agreement of its respective trust and do not require the consent or approval of any other Person. Each Transaction Document to which the Owner Trustee or the Indenture Trustee is a party has been duly executed and delivered by the Owner Trustee or the Indenture Trustee, respectively, and constitutes the legal, valid and binding obligation of the Owner Trustee or the Indenture Trustee, respectively, enforceable against the Owner Trustee or the Indenture Trustee, respectively, in accordance with its terms.

6. Immediately prior to the execution and delivery of the Transaction Documents, APS owned the property to be transferred by APS to Owner Trustee under the Transaction Documents. Based on our knowledge, without independent investigation, we have no reason to believe this assumption is invalid. The assumption in this Paragraph 6 does not apply to the opinion in the first sentence of Section 14 of this legal opinion.

7. Amendment Number 10 to the ANPP Participation Agreement has been duly authorized, executed and delivered by, constitutes the legal, valid and binding agreement of, and is enforceable against, each of the parties thereto (other than APS).

8. The Transaction Documents accurately and completely set forth all agreements, arrangements and understandings of the parties thereto with respect to the transaction described in and contemplated by the Transaction Documents.

9. The Facility Lease is a "lease" and not a financing arrangement for Federal income tax purposes and an "operating lease" and not a "capital lease" for financial reporting purposes under Financial Accounting Standards Board Statement 13 and will be so treated and reported for such purposes by APS and Owner Trustee.

Based on the foregoing and subject to the qualifications set forth herein, it is our opinion as of the date hereof that:

1. APS is a corporation duly organized and validly existing in good standing under the laws of the State of Arizona and has the corporate power and authority to carry on its business as presently conducted, to own or hold under lease its properties and to enter into and perform its obli-

gations under the Participation Agreement, the Reimbursement Agreement and each other Transaction Document to which APS is a party. APS is duly qualified and in good standing to do business as a foreign corporation in the State of New Mexico and has not failed to qualify to do business or to be in good standing in any other jurisdiction where failure so to qualify or be in good standing would materially and adversely affect the financial condition or operations of APS or its ability to perform any obligations under the Participation Agreement, the Reimbursement Agreement or any other Transaction Document to which APS is a party.

2. The execution, delivery and performance by APS of the Participation Agreement and each other Transaction Document to which APS is a party have been duly authorized by all necessary corporate action on the part of APS and do not require the consent or approval of the stockholders of APS or any trustee or holder of any indebtedness or other obligation of APS, other than such consents and approvals as have been duly obtained, given or accomplished.

3. The Participation Agreement and each other Transaction Document to which APS is a party have been duly executed and delivered by APS and constitute the legal, valid and binding agreement of APS, enforceable against APS in accordance with their respective terms (other than the Facility Lease, which is discussed in Section 16 below). The opinions set forth in this Section 3 are subject to the qualifications that (i) enforceability of the Participation Agreement and the other Transaction Documents to which APS is a party in accordance with their respective terms may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting enforcement of creditors' or lessors' rights generally, as well as general principles of equity and the availability of equitable remedies, and (ii) certain laws and judicial decisions may affect the enforceability of certain rights and remedies provided in the Transaction Documents. With respect to the latter qualification, however, we are of the opinion that none of such laws now in effect and none of such judicial decisions presently existing make the rights and remedies provided in the Transaction Documents, taken as a whole, inadequate for the realization of the benefits of the Transaction Documents.

4. Neither the execution, delivery or performance by APS of its obligations pursuant to the Participation Agreement or any other Transaction Document to which APS is a

party, nor the consummation by APS of the transactions contemplated thereby, nor compliance by APS with the provisions thereof, conflicts with, or results in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or Bylaws of APS or, to the best of our knowledge after due inquiry, any Affiliate of APS, or, to the best of our knowledge after due inquiry, any indenture, mortgage, lease or any other agreement or instrument to which APS or any Affiliate of APS is a party or by which the property of APS or any Affiliate of APS is bound, or results in the creation or imposition of any Lien (other than Permitted Liens) upon any property of APS or any Affiliate of APS.

5. All Arizona Governmental Action which is required in connection with the execution, delivery or, as of the date hereof, performance by APS of its obligations pursuant to, or the consummation by APS of the transactions contemplated by, the Participation Agreement and any other Transaction Document to which APS is a party, have been duly obtained, given or accomplished, except that our opinion in this Section 5 does not relate to the recording or filing of any Transaction Documents, although we hereby confirm that we have submitted for recordation or filing the documents specified in Schedule 5 to the Participation Agreement (except those documents specified in Part IIC to such Schedule).

6. APS holds such valid franchises, certificates of convenience and necessity, licenses, and permits as are necessary with respect to the maintenance and operation of its property and business as now conducted, except that (a) APS from time to time makes minor extensions of its system prior to the time a related franchise, certificate, license, or permit is procured, (b) from time to time communities already being serviced by APS become incorporated and considerable time may elapse before a franchise is procured, (c) certain franchises may have expired prior to the renegotiation thereof, (d) APS may not have obtained certain permits or variances relating to the environmental requirements described under "Environmental Requirements" in Item 1 in APS's Report on Form 10-K for the fiscal year ended December 31, 1985, and (e) certain minor defects and exceptions may exist which, individually and in the aggregate, are not deemed material.

7. Except as disclosed in the financial statements to which reference is made in Section 10(a)(11) of the Participation Agreement and in the reports to which reference

is made in Section 10(a)(12) of the Participation Agreement, there is no action, suit, investigation or proceeding pending or, to our knowledge after due inquiry, threatened against APS before any federal or Arizona court, arbitrator or administrative or governmental body which questions the validity or enforceability of the Participation Agreement, any other Transaction Document in effect on the date hereof, or the ANPP Participation Agreement, or which, individually or in the aggregate, if decided adversely to the interests of APS, would have a material adverse effect on the business or financial condition of APS or materially and adversely affect the ability of APS to perform its obligations under the Participation Agreement or any other Transaction Document in effect on the date hereof to which APS is a party.

8. The lien of the Existing Mortgage does not extend to contract rights of APS under the Transaction Documents (other than the Facility Lease) or to the Generation Entitlement Share related to the Undivided Interest.

9. Under Arizona Applicable Law, neither the Loan Participants, Funding Corporation, the Equity Participant, the Bank nor FNB (in its individual capacity and as Owner Trustee) will be or become, solely by reason of the activities contemplated by the Transaction Documents or the Reimbursement Agreement prior to the expiration or termination of the Facility Lease, subject to regulation as a public service corporation, public utility, or a public utility holding company by any Arizona public utility commission or other Arizona regulatory body, authority or group (including, without limitation, the Arizona Corporation Commission), provided, however, that we express no opinion regarding the effect of (i) any transfer of ownership of the Undivided Interest or the Real Property Interest by the Owner Trustee, (ii) termination or expiration of the Facility Lease and the taking of possession by the Owner Trustee or any other Person of an interest in Unit 2, (iii) APS's providing of transmission services for the Owner Trustee or any other Person owning the Undivided Interest or the Real Property Interest, or (iv) any exercise of remedies or other rights by any Person in connection with taking possession of an interest in Unit 2.

10. APS is a "subsidiary company" of a "holding company," AZP Group, Inc., and an "affiliate" of a "holding company," as such terms are defined in the Holding Company Act, but APS is exempt from all provisions of the Holding

Company Act and the rules thereunder (except Section 9(a)(2) of the Holding Company Act).

11. The execution, delivery and performance of the Transaction Documents or the Reimbursement Agreement by the parties thereto do not violate the Atomic Energy Act, as now in effect, the NRC regulations now in effect, or any order of the NRC now in effect, provided that such parties comply with the terms and conditions of the License. No Governmental Action by or with respect to the NRC is or will be required in connection with the execution, delivery or performance by APS of the Participation Agreement, the Reimbursement Agreement, the Facility Lease, the Assignment and Assumption or any other Transaction Document to which it is a party, except (i) such Governmental Actions as may be required pursuant to the express terms of the License; (ii) such other Governmental Actions by or with respect to the NRC as have been duly obtained, given or accomplished on or before the date hereof; (iii) such Governmental Actions of or with respect to the NRC as it may determine after the Closing Date under existing law to be necessary to protect the public health and safety in connection with the construction, improvement, maintenance, operation, decommissioning or retirement from service by the Licensees described in the License of any portion of Unit 2 or PVNGS or otherwise with respect to Unit 2 or PVNGS; and (iv) such other Governmental Actions as may be required under Applicable Law not now in effect. The exercise by the Lessor and the Equity Participant of their respective rights and remedies under the Facility Lease and the other Transaction Documents, under the circumstances and for the purposes therein set forth, will not violate the License or the terms and conditions of such License, except to the extent that the NRC shall determine that the exercise of such rights and remedies will or may adversely affect the public health and safety.

12. The transfer of property and interests in property by APS to the Owner Trustee pursuant to the Participation Agreement, the Bill of Sale, the Deed, and the Assignment and Assumption is not a fraudulent conveyance under the law of the State of Arizona, provided, however, that this opinion, in so far as it relates to A.R.S. Section 44-1061 and any common law vendor-in-possession fraudulent conveyance doctrine, is subject to the following comments. A.R.S. Section 44-1061 provides:

"A. A sale made by a vendor of goods and chattels in his possession or under his

control, or an assignment of goods and chattels, unless the sale or assignment is accompanied by an immediate delivery and followed by an actual and continued change of possession of the things sold or assigned, is *prima facie* evidence of fraud against creditors of the vendor, or creditors of the person making the assignment, or subsequent purchasers in good faith.

"B. The term 'creditors' includes all persons who are creditors of the vendor or assignor at any time while such goods and chattels are in his possession or under his control."

The Arizona court decisions interpreting A.R.S. Section 44-1061 arose in the context of tangible property in the actual possession of the seller. These decisions suggest that open, visible and unequivocal indications that there has been a change of ownership would be sufficient to overcome the *prima facie* evidence of fraud established by Section 44-1061. See, e.g., *Nolte v. Winstanley*, 16 Ariz. 327, 145 P. 246 (1914). Unfortunately, this precedent is not very helpful in the context of the present transaction. In addition, the court decisions under A.R.S. Section 44-1061 are equivocal as to the effect of recording or filing transfer documents. *Nolte v. Winstanley, supra*; and *Leibes v. Steffy*, 4 Ariz. 11, 32 P. 261 (1893). Notwithstanding this equivocation, as to a subsequent encumbrancer of any personal property which is subject to Article 9 of the Uniform Commercial Code as in effect in Arizona, which is described in the three (3) UCC-1 Financing Statements, dated August 18, 1986 between APS, as the lessee, and Owner Trustee, as lessor, filed with the Secretary of State of Arizona and the County Recorder, Maricopa County, State of Arizona (the "Lease Financing Statements") and in which a security interest may be perfected by filing of a financing statement within Arizona, we believe that the filing of the Lease Financing Statements should be sufficient to overcome the *prima facie* evidence of fraud to the extent the description of such property in the Lease Financing Statements is accurate and complete. In addition, as to future creditors with actual knowledge of the transfers in the Deed, the Bill of Sale, and the Assignment and Assumption prior to extending or committing to extend credit, we believe that such knowledge should overcome the *prima facie* evidence of fraud in A.R.S. Section 44-1061.

13. Neither the execution and delivery by APS of, nor the performance by APS of its obligations under, any Transaction Document to which it is a party, conflicts with, or results in a breach of any statute, ordinance, governmental rule or regulation of the State of Arizona or Maricopa County, except that our opinion in this Section 13 does not relate to any conflict or breach after the date hereof as a result of (i) the construction, improvement, maintenance, use, possession, operation, decommissioning or retirement from service of any portion of Unit 2 or PVNGS or otherwise with respect to Unit 2 or PVNGS or APS's or the Operating Agent's involvement therewith, APS's duties and obligations as an ANPP Participant under any of the ANPP Project Agreements, or APS's duties and obligations as Agent under the Assignment and Assumption; (ii) securities and taxation laws of any Arizona Governmental Authority; (iii) any Releveraging, Refunding, or Reoptimization described in Sections 2(d), 2(e) and 2(f) of the Participation Agreement; (iv) any Supplemental Financing pursuant to Section 8(f) of the Facility Lease; (v) any action taken by APS pursuant to Section 10(b)(2) of the Participation Agreement or any similar provision in the Participation Agreement or any other Transaction Document; (vi) any involvement by APS in connection with any transfer of ownership of the Undivided Interest or the Real Property Interest by the Owner Trustee or the taking of possession of the Undivided Interest or the Real Property Interest by Owner Trustee or any other Person upon expiration or termination of the Facility Lease or otherwise; (vii) APS providing transmission services for the Owner Trustee or any other Person owning the Undivided Interest or the Real Property Interest or ceasing to serve as Agent pursuant to the Assignment and Assumption; (viii) any action by APS pursuant to Article VII of the Assignment and Assumption; (ix) Lessor or any other Person, other than APS, receiving the Generation Entitlement Share of APS pursuant to Section 19 of the Facility Lease or any other provision of any Transaction Document; or (x) any payment by APS pursuant to Sections 14(b) or 16 of the Participation Agreement or any similar provision in the Participation Agreement or any other Transaction Document.

14. Assuming that any choice of law provision in favor of the law of a state other than the State of Arizona is disregarded therein, (i) the Deed, the Bill of Sale and the Assignment and Assumption are in sufficient form to convey from APS to Owner Trustee the interests in property described therein and for recording under the law of the State

of Arizona and (ii) the Indenture is in sufficient form to grant from Owner Trustee to Indenture Trustee the security interest and mortgage described therein and for recording under the law of the State of Arizona. The Deed, the Bill of Sale, the Assignment and Assumption, the Facility Lease and the Indenture when duly executed, acknowledged and delivered, must each be recorded in the Office of the Recorder of Maricopa County, Arizona, together with an Affidavit of Legal Value pursuant to A.R.S. Section 42-1612 with respect to any such document transferring title to real estate (other than leases or easements). Precautionary financing statements pursuant to A.R.S. Section 47-9408 and financing statements naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate must be filed in the office of the Arizona Secretary of State and recorded in the Office of the Recorder of Maricopa County, Arizona. We hereby confirm that we have submitted for recordation or filing the documents referred to in the two (2) preceding sentences. Upon the completion of such recordings and filings and except as explained below, no other filings or recordings in Arizona are required to establish, preserve, perfect, and protect (i) the Owner Trustee's rights and interests (including, without limitation, any security interest which may be deemed to be created by the Facility Lease) in and to the Undivided Interest and the Real Property Interest and (ii) the security interest of the Indenture Trustee in the Lease Indenture Estate, and no additional recordation is required to continue the effectiveness of such recordings, provided that our opinion in this Section 14 is limited to property constituting the Undivided Interest, the Real Property Interest and the Lease Indenture Estate that is either real property under the law of the State of Arizona or property subject to Article 9 of the Uniform Commercial Code (as in effect in Arizona) in which a security interest may be perfected by the filing of a financing statement within the State of Arizona. In addition, no additional financing statements, other than those filed with the Secretary of State of Arizona and recorded in the Office of the County Recorder of Maricopa County, Arizona, are required to be filed in order to continue the effectiveness thereof except that continuation statements are required to be filed with respect to such financing statements within each of the six-month periods preceding the expiration of each six-year period after the respective dates of filing. We express no opinion regarding the form for conveyance, the transfer or the perfection of rights in any Capital Improvements or regarding filings or recordings that may be required

under the laws of any other state, under federal law or by reason of the application of the conflict of laws rules set forth in A.R.S. Section 47-9103. To the extent any recorded or filed Transaction Document refers to or incorporates by reference any other document (for definitional purposes or otherwise) not recorded or filed in the same location or if recorded or filed, not identifying the date and instrument or file number of such document incorporated by reference, our opinion in this Section 14 excludes the effect, if any, of such reference or incorporation by reference. In giving our opinion in this Section 14 we have assumed that the description of the Undivided Interest, the Real Property Interest and the Lease Indenture Estate in the Transaction Documents is accurate and complete.

15. You have requested that we advise you whether an Arizona court would give effect to the choice of law provision in favor of the law of the State of New York in each Transaction Document, other than the Deed, the Bill of Sale, the Assignment and Assumption, and the Facility Lease. There is no Arizona case stating that an Arizona court will follow the choice of law provision of the parties to a contract. However, the Supreme Court of Arizona has consistently ruled that where it is not bound by a previous decision or by legislative enactment it will follow the rules in the *Restatements of the Law* including the *Restatements of Conflict of Laws*. *Smith v. Normat*, 51 Ariz. 134, 75 P.2d 38 (1938); *Western Coal & Min. Co. v. Hilvert*, 63 Ariz. 171, 160 P.2d 331 (1945); and *Taylor v. Security National Bank*, 20 Ariz. App. 504, 514 P.2d 257 (1973). Section 187 of the *Restatement (Second) Conflict of Laws* provides that the parties to a contract may stipulate to their choice of law to govern the contract and that the laws of the state chosen will be applied unless (i) the particular issue is one which the parties could not have resolved by an explicit provision in their agreement directed to that issue, and (ii) either:

"(a) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or

"(b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the

chosen state in the determination of the particular issue and which, under the rule of Section 188, would be the state of the applicable law in the absence of an effective choice of law by the parties."

We believe that the State of New York has a "substantial relationship" to the parties or the transaction with respect to the documents covered by the opinion in this Section 15 and that with respect to such documents there is a reasonable basis for the choice of law of the State of New York because at least one of the parties to such documents is located in the State of New York and such documents have been substantially negotiated within and from the State of New York and have been executed and delivered within the State of New York. Thus, the effectiveness of the choice of law provisions in these documents will depend upon whether, as to the particular issue in question, (i) there would be a difference in the applicable substantive law of the State of New York, on the one hand, and the law of the State of Arizona or another state, on the other hand, (ii) the resolution of such issue under the law of the State of New York would be contrary to a fundamental policy of the State of Arizona or such other state, (iii) the State of Arizona or such other state would have a materially greater interest than the State of New York in the determination of the particular issue and (iv) under Section 188 of the *Restatement (Second) Conflict of Laws*, the law of the State of Arizona or such other state would be the applicable law.

16. Assuming an Arizona court were not to give effect to the choice of law provision in the Facility Lease in favor of the law of the State of New York and were to apply the law of the State of Arizona (other than choice of law rules), the Facility Lease is the legal, valid, and binding obligation of APS and is duly enforceable against APS in accordance with its terms:

(a) Except as limited by applicable bankruptcy, insolvency, moratorium, reorganization, and similar laws of general application;

(b) Except as limited by equitable principles of general application; and

(c) Except as limited by other applicable laws or general principles of law that may render unenforceable

certain provisions of the Facility Lease, provided, however, that (i) if Owner Trustee does not violate the terms of the License referenced in Section 11 of this legal opinion and Owner Trustee fulfills the duty, if applicable, to mitigate losses, such limitations will not interfere with the enforcement by Owner Trustee of the obligations of APS to pay Basic Rent as provided in Section 3(a) of the Facility Lease as the payments of Basic Rent become due on each Basic Rent Payment Date prior to termination of the Facility Lease and without acceleration or advancement thereof and (ii) Owner Trustee may obtain the return of the Undivided Interest and the Real Property Interest upon termination or expiration of the Facility Lease, except in the case of each of (i) and (ii) for the economic consequences of any procedural delays that may result from such limitations.

Anything in this opinion to the contrary notwithstanding, we express no opinion concerning (i) the ownership of, or legal or equitable title to, any property, (ii) whether the property described and referred to in the Transaction Documents is personal property or real property or whether any severance or other provision in the Transaction Documents purporting to make certain property personal property is effective, or (iii) the priority of the interest of any person in any property or interest in property.

In rendering the opinions set forth above, we have relied as to all matters relating to the law of the State of New York, solely upon the opinion of Mudge Rose Guthrie Alexander & Ferdon, Special Counsel for APS, delivered pursuant to Section 11(a)(19) of the Participation Agreement, as to which law we have, with your consent, made no independent investigation. Subject to the foregoing qualification, the above opinions are limited to the laws of the State of Arizona as in effect on the date of this opinion and we express no opinion as to the applicability or effect of federal law, except as set forth in Sections 10 and 11 of this opinion and as federal law is in effect on the date of this opinion, or the law of any state other than Arizona. This opinion is rendered to you solely in connection with the transactions described in and contemplated by the Transaction Documents. This opinion is not to be referred to, or quoted in, any document, report, or financial statement or filed with, or delivered to, any governmental entity or other person or entity, without our prior written consent.

Very truly yours,

Sheel Wilmer

SCHEDULE

Security Pacific Capital Leasing Corporation
as Equity Participant
Four Embarcadero Center
Executive Offices (Suite 1200)
San Francisco, California 94111
Attention: Manager, Operations Department/LEV

PVNGS Funding Corp., Inc.,
as Loan Participant
Corporate Trust Center
1209 Orange Street
Wilmington, Delaware 19801

Arizona Public Service Company
as Lessee
North Central Avenue
P.O. Box 53999
Phoenix, Arizona 85072-3999

The First National Bank of Boston,
as Owner Trustee
100 Federal Street
Boston, Massachusetts 02110

Chemical Bank,
as Indenture Trustee
55 Water Street
New York, New York 10041

Mudge Rose Guthrie Alexander & Ferdon
180 Maiden Lane
New York, New York 10038

Bank of America National Trust
and Savings Association
as Agent for the Original Loan Participants
555 South Flower Street
Los Angeles, California 94104

EXHIBIT A

ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (APS), hereby certifies the following to Snell & Wilmer in connection with their giving a legal opinion (Legal Opinion) with respect to the sale and leaseback transaction that is the subject matter of the Participation Agreement (Participation Agreement), dated as of August 1, 1986, among the Equity Participant identified on Schedule 1 attached hereto and incorporated herein, PVNGS Funding Corp., Inc., Bank of America National Trust and Savings Association (for itself and as Agent), The First National Bank of Boston (in its individual capacity and as Owner Trustee), Chemical Bank (in its individual capacity and as Indenture Trustee), and APS (all capitalized terms used herein and not otherwise defined herein will have the meanings ascribed to them in the Legal Opinion):

1. The relationship of APS and Owner Trustee in respect of each of the following Transaction Documents intended, agreed to, and understood by APS, Owner Trustee, and each other party to any of the Transaction Documents is as follows:

(a) The relationship of APS and Owner Trustee in respect of the Deed and Bill of Sale and the Assignment and Assumption is one of seller and purchaser, respectively; and

(b) The relationship of Owner Trustee and APS in respect of the Facility Lease is one of lessor and lessee, respectively.

2. Each and all of the operative provisions of the Transaction Documents, in general, and the following basic aspects of the transaction described in and contemplated by the Transaction Documents, in particular, are intended, agreed to, and understood by each and all of APS, Owner Trustee, Equity Participant, and each other party to any of the Transaction Documents:

(a) The Deed and Bill of Sale and the Assignment and Assumption are absolute, unconditional and indefeasible transfers of the property and interests in property described therein;

(b) The Undivided Interest is leased back by Owner Trustee to APS for an extendable term as provided in the Facility Lease, subject to the early termination and other provisions of the Facility Lease;

(c) APS's obligation to pay rent under the Facility Lease is absolute and unconditional as set forth in Section 4 of the Facility Lease; and

(d) The property and interests in property transferred by APS to Owner Trustee by the Deed and Bill of Sale and the Assignment and Assumption are to be owned by Owner Trustee upon expiration or earlier termination of the Facility Lease without further consideration passing from Owner Trustee to APS.

3. The Transaction Documents are an accurate and complete statement of the agreements, arrangements, and understandings of the parties thereto with respect to the transaction described in and contemplated by the Transaction Documents.

4. From the first contact of APS, Equity Participant and each other party to any Transaction Document and continuing through all discussions and negotiations among the parties to the Transaction Documents, the transaction described in and contemplated by the Transaction Documents has been intended and understood by APS, Equity Participant, and each other such party to be a sale and leaseback transaction.

IN WITNESS WHEREOF, APS has caused this Certificate to be executed on its behalf by its duly authorized officer as of August 18, 1986.

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona corporation

By: 

Its: Vice President

MUDGE ROSE GUTHRIE ALEXANDER & FERDON EXHIBIT B-3

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12, RUE DE LA PAIX
75002, PARIS, FRANCE
(1) 42. 61. 57. 71

August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

SALE AND LEASEBACK OF AN UNDIVIDED INTEREST IN
PALO VERDE NUCLEAR GENERATING STATION UNIT 2

Dear Sirs:

We have acted as special New York counsel for Arizona Public Service Company, an Arizona corporation (APS), in connection with the transactions contemplated by (i) the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among Security Pacific Capital Leasing Corporation, a Delaware corporation, as Equity Participant, PVNGS Funding Corp., Inc., a Delaware corporation (Funding Corp), Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants listed on Schedule 1 to the Participation Agreement, The First National Bank of Boston, a national banking association, individually and as Owner Trustee, Chemical Bank, a New York banking corporation, individually and as Indenture Trustee, and APS and (ii) the Reimbursement Agreement, dated as of August 1, 1986 (the Reimbursement Agreement), between APS and Morgan Guaranty Trust Company of New York, a New York trust company (the Bank). All capitalized terms used herein and not otherwise defined herein or in Section 1 to the Reimbursement Agreement shall have the meanings assigned thereto in Appendix A to the Participation Agreement. This opinion is being delivered pursuant to Section 3(b)(ii) of the Reimbursement Agreement.

As such counsel we have examined originals or copies, certified or otherwise identified to our satisfaction, of such corporate records, agreements and other instruments, certificates, opinions, correspondence with public officials, certificates of officers,

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management personnel and representatives of APS, and such other documents, as we have deemed necessary or advisable for the purposes of rendering the opinions set forth herein.

Based on the foregoing and subject to the qualifications set forth below, we are of the opinion that:

(1) The Reimbursement Agreement and each Transaction Document to which APS is a party have been duly executed and delivered by APS, and, assuming the due authorization, execution and delivery thereof by the other parties thereto (other than Funding Corp), the Reimbursement Agreement and each Transaction Document to which APS is a party constitute the legal, valid and binding agreements of APS, enforceable against APS in accordance with their respective terms.

(2) Neither the execution, delivery or performance by APS of the Reimbursement Agreement or any Transaction Document to which APS is a party, nor the consummation by APS of the transactions contemplated thereby, nor compliance by APS with the provisions thereof, conflicts with, or results in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or By-Laws of APS, or any Federal or New York Applicable Law.

(3) No Governmental Action under any Federal or New York law now in effect is required in connection with the execution, delivery or performance by APS of, or the consummation by APS of the transactions contemplated by, the Reimbursement Agreement or any Transaction Document to which APS is a party, except such Federal and New York Governmental Actions (i) as have been duly obtained, given or accomplished, (ii) as are routine in nature and that cannot be obtained, or are not normally applied for, prior to the time they are required, (iii) as may be required to be obtained, given or accomplished from time to time in connection with the maintenance, use, possession, operation or improvement of Unit 2 or otherwise with respect to Unit 2 and APS's or the Operating Agent's involvement therewith, (iv) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (v) as may be required in consequence of the issuance, sale or exchange and delivery of or any obligations issued under and pursuant to any Collateral Trust Indenture, (vi) as may be required by existing Applicable Law on and after termination or expiration of the Facility Lease, or (vii) as may be required under Federal or New York law not now in effect. No Federal or New York Governmental Action is or will be required (a) solely

by virtue of the participation by the Bank or any Participant in the consummation of the transactions contemplated by the Reimbursement Agreement to take place on the date hereof or by the Owner Trustee, the Indenture Trustee, the Equity Participant, Funding Corp or any Loan Participant in the consummation of the transactions contemplated by the Transaction Documents to take place on the date hereof or (b) to be obtained by any of such Persons during the term of the Facility Lease with respect to Unit 2 except, in each case, such Federal or New York Governmental Actions (i) as have been duly obtained, given or accomplished, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of or any obligations issued under and pursuant to any Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required under the Holding Company Act in the event that no proper filing of Form U-7D with the SEC is made on or within 30 days after the date hereof, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person under Section 16 of the Facility Lease or otherwise in connection with taking possession of an interest in Unit 2.

(4) So long as the Facility Lease is in effect, assuming the proper filing of Form U-7D with the SEC on or within 30 days after the date hereof, under Federal law now in effect, neither the Bank, any Loan Participant, the Equity Participant, FNB nor the Owner Trustee will be or become, solely by reason of either its entering into the Reimbursement Agreement or any Transaction Document to which any of them is a party, or the transactions contemplated thereby, subject to regulation as an electric utility company, an electric utility, a public-utility company or corporation, a public utility, a holding company, a public utility holding company, an electric corporation, or a utility company or corporation by any Federal or New York public utility commission or other regulatory body, authority or group (including, without limitation, the SEC and the FERC).

(5) APS is not an "investment company", or a company "controlled" by an "investment company"; within the meaning of the Investment Company Act.

The opinions set forth above are subject to the qualifications that (i) enforceability of the Reimbursement Agreement

and the Transaction Documents to which APS is a party in accordance with their respective terms may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting enforcement of creditors' or lessors' rights generally, as well as general principles of equity, and (ii) certain laws and judicial decisions may affect the enforceability against APS of certain rights and remedies provided in the Transaction Documents. With respect to the latter qualification, however, we are of the opinion that none of such laws now in effect and none of such judicial decisions make the rights and remedies provided in the Transaction Documents, taken as a whole, inadequate for the realization of the benefits of the Transaction Documents.

This opinion is limited to the laws of the State of New York and the Federal laws of the United States of America; however we express no opinion as to any matters relating to the Atomic Energy Act or the Nuclear Waste Act.

Very truly yours,

Mudge Rose Guthrie Alexander & Ferdon

DAVIS POLK & WARDWELL

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WRITER'S DIRECT NUMBER:

EXHIBIT C

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RICHARD B. SMITH
EDWIN DEANE LEONARD
BRUCE W. NICHOLS
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ALAN DEAN
JOHN R. ETTINGER
RICHARD MOE 'O C. BAY 'ONEL
JAMES O. PHYFE
E. WAIGE WARNER, JR.

August , 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Dear Sirs:

We have acted as your counsel in connection with the preparation, execution and delivery of the: Reimbursement Agreement dated as of August 1, 1986 (the "Reimbursement Agreement") between Arizona Public Service Company, an Arizona corporation (the "Company"), and Morgan Guaranty Trust Company of New York (the "Bank"). Terms defined in the Reimbursement Agreement are used herein as therein defined.

We have examined originals or copies, certified or otherwise identified to our satisfaction, of such documents, corporate records, certificates of public officials and other instruments and have conducted such other investigations of fact and law as we have deemed necessary or advisable for purposes of this opinion.

Upon the basis of the foregoing, we are of the opinion that the Reimbursement Agreement constitutes a valid and binding agreement of the Company enforceable in accordance with its terms except as (i) the enforceability thereof may be limited by bankruptcy, insolvency or similar laws affecting creditors' rights generally and (ii) rights of acceleration and the availability of equitable remedies.

may be limited by equitable principles of general applicability.

In rendering the foregoing opinion, we have relied, without independent investigation, as to all matters of Arizona law upon the opinion, dated the date hereof, of Snell & Wilmer, counsel for the Company, delivered to you pursuant to Section 3(b)(i) of the Reimbursement Agreement, and our opinion is subject to the qualifications and exceptions therein expressed.

Very truly yours,

Davis Polk & Wardwell

Rates

On February 13, 1986, the date Unit 1 of the Palo Verde Nuclear Generating Station attained commercial operation as defined by the Arizona Corporation Commission (the "ACC"), the Company ceased accruing allowance for funds used during construction ("AFC") with respect to Unit 1 and the facilities common to all three Palo Verde Units (the "Common Facilities") in the amount of approximately \$6 million per month. In addition, the Company began expensing the cost of owning, operating and maintaining its 29.1% share of Unit 1 and the Common Facilities, currently totalling approximately \$5 million per month. Absent adequate and timely rate relief from the ACC, the Company expects these developments to continue to adversely affect its earnings.

On July 24, 1986, ACC issued an order concerning the purchased power and fuel adjustment mechanism ("PPFAM") of the Company in the "Phase I" hearing of the rate case in which the Company requested an increase in annual retail rates premised on Unit 1 of Palo Verde being fully included in the Company's rate base. To permit the Company to recover these fuel costs that the ACC found reasonable, the order authorized the Company to increase its "base fuel" charge to \$.016033 per kilowatt hour and established the PPFAM charge at \$.003099 per kilowatt hour (the "PPFAM Charge"), both of which became effective August 1, 1986. At June 30, 1986, the Company had under-collected fuel and purchased power costs of approximately \$66.2 million. Through the operation of the PPFAM Charge, the Company will recover approximately \$41.8 million of this amount over a period of approximately one year. The ACC disallowed recovery of the remainder of under-collected fuel and purchased power costs, approximately \$24.4 million, due to the Company's temporary sale of generating output from Unit 4 of the Cholla Plant to another utility. The Company, on August 11, 1986, filed a motion seeking reconsideration and rehearing of the ACC's order. A temporary PPFAM charge of \$.004 per kilowatt hour, designed to reduce the Company's under-collected fuel and purchased power costs, had been in effect since September 1985, pending the "Phase I" determination.

TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND
ASSIGNMENT OF FACILITY LEASE

Dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON, not
in its individual capacity, but solely
as Owner Trustee under a Trust
Agreement dated as of August 1,
1986, with EMERSON FINANCE CO.

and

CHEMICAL BANK,
as Indenture Trustee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

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TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF FACILITY LEASE dated as of August 1, 1986, between THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as trustee under a Trust Agreement dated as of August 1, 1986 between FNB, whose address is 100 Federal Street, Boston, Massachusetts 02110, with Emerson Finance Co., and CHEMICAL BANK, a New York banking corporation, whose address is 55 Water Street, New York, New York 10041.

W I T N E S S E T H:

WHEREAS, the Owner Trustee has entered into a Participation Agreement, dated as of August 1, 1986 among the Equity Participant, PVNGS Funding Corp., Inc., a Delaware corporation, Bank of America National Trust and Savings Association, a national banking association, Arizona Public Service Company, an Arizona corporation, and the Indenture Trustee;

WHEREAS, the Owner Trustee, acting on behalf of the Equity Participant, pursuant to the Trust Agreement and the Participation Agreement, intends to purchase the Undivided Interest and the Real Property Interest from APS and lease the Undivided Interest and the Real Property Interest to APS pursuant to the Facility Lease;

WHEREAS, in order to finance a portion of the Purchase Price of the Undivided Interest, the Owner Trustee desires to issue its promissory notes hereunder with such promissory notes to be substantially in the form of Exhibit A hereto;

WHEREAS, in the circumstances contemplated by Sections 2(d) and 2(e) of the Participation Agreement, the Owner Trustee may desire to issue Refunding Notes (together with any other Notes issued hereunder other than the Initial Series Notes, the Additional Notes) or to increase the principal amount of the Outstanding Refunding Notes or to change the amortization of either or both thereof;

WHEREAS, in order to finance the Supplemental Financing Amount of Capital Improvements and to refund notes of any series previously issued, the Owner Trustee may desire to issue additional Refunding Notes hereunder secured on a pari passu basis with other Notes Outstanding from time to time;

WHEREAS, in order to secure the obligations referred to herein, the Owner Trustee desires to grant to the Indenture Trustee the security interest and realty mortgage herein provided and the parties hereto desire that this Indenture be regarded (i) as a "security agreement" and as a "financing statement" for such security agreement under the Uniform Commercial Code and (ii) to the extent that the Undivided Interest and the Real Property Interest constitute fixtures or real property, as a realty mortgage;

NOW, THEREFORE, in consideration of the premises, of the acceptance by the Indenture Trustee of the trusts hereby created and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

CONSTRUCTION, GOVERNING LAW, INTERPRETATION AND DEFINITIONS

SECTION 1.1. Governing Law.

This Indenture (i) is being executed and delivered in the State of New York, (ii) shall be deemed to be a contract made in such State and (iii) for all purposes shall be construed in accordance with and governed by the laws of the State of New York, except to the extent to which the laws of the State of Arizona are mandatorily applicable hereto.

SECTION 1.2. Headings and Table of Contents.

The division of this Indenture into articles and sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Indenture.

SECTION 1.3. Definitions; Construction of References.

In this Indenture, unless the context otherwise requires:

(a) the term this Indenture means this instrument together with all exhibits, appendices and schedules hereto as originally executed and as it may from time to time be supplemented or amended by one or more indentures supplemental hereto pursuant to the provisions hereof;

(b) all references in this instrument to designated Articles; Sections and other subdivisions are to designated Articles, Sections and other subdivisions of this instrument unless otherwise indicated;

(c) all accounting terms not otherwise defined herein shall have the meanings assigned to them in accordance with generally accepted accounting principles; and

(d) capitalized terms used herein which are not otherwise defined herein shall have the meanings set forth in Appendix A hereto (as such Appendix may be supplemented or amended pursuant to, and in accordance with, the terms hereof), and the rules of construction set forth in Appendix A hereto shall be applicable hereto.

SECTION 1.4. Disclosure of Beneficiaries.

Pursuant to Arizona Revised Statutes Section 33-401, (i) the beneficiary of the Trust Agreement is Emerson Finance Co., a Delaware corporation, whose address is 111 East Prospect, Stamford, CT 06904: Attention: President and (ii) the beneficiary of this Indenture is (1) during the period that the Initial Series Notes are Outstanding, the Agent, whose address is 555 South Flower Street, Los Angeles, California 90071, (2) during the period that the Loan Participant is the Funding Corp, PVNGS Funding Corp., Inc., whose address is Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 19801, Attention: President and, by pledge and assignment, Chemical Bank, as trustee under the Collateral Trust Indenture, whose address is 55 Water Street, New York, New York 10041: Attention of Corporate Trustee Administration and (3) during any period that the Loan Participant is other than the Agent or the Funding Corp, at the address set forth in the applicable indenture supplemental to this Indenture. Copies of the Trust Agreement and this Indenture are available for inspection at the Indenture Trustee's Office.

ARTICLE II

SECURITY

SECTION 2.1. Grant of Security Interest; Mortgage.

As security for the due and punctual payment of the principal of and premium, if any, and interest on the Notes according to their respective terms and effect and the performance and observance by the Owner Trustee of all the covenants and agreements made by it or on its behalf in the Notes, the Participation Agreement and this Indenture, the Owner Trustee does by its execution and delivery hereof hereby grant a security interest in and grant, bargain, convey, warrant, assign, transfer, mortgage, pledge and set over unto the Indenture Trustee, and to its successors and assigns in trust, for the ratable benefit of the Holders of the Notes, the following (the Lease Indenture Estate):

(1) all right, title and interest of the Owner Trustee in and to the Undivided Interest and the Real Property Interest;

(2) all right, title and interest of the Owner Trustee in, to and under (a) the Purchase Documents, (b) the ANPP Participation Agreement, (c) the Assignment and Assumption Agreement and (d) the Facility Lease (collectively the Granting Clause Documents), and all sums payable to the Owner Trustee with respect thereto, including, without limitation, (x) all amounts of Rent (including, without limitation, Basic Rent and Supplemental Rent) and payments under and pursuant to Sections 13(c) and 16 of the Facility Lease) (the Assigned Payments), insurance proceeds and condemnation, requisition and other awards and payments of any kind for or with respect to any part of the Lease Indenture Estate as contemplated in or by the Granting Clause Documents and (y) all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of any Granting Clause Document, as well as all rights, powers

and remedies on the part of the Owner Trustee, whether arising under any Granting Clause Document or by statute or at law or equity or otherwise, arising out of any Indenture Event of Default;

(3) all moneys and securities deposited or required to be deposited with the Indenture Trustee pursuant to any term of this Indenture and held or required to be held by the Indenture Trustee hereunder;

(4) all rents (including Rent), issues, profits, products, revenues and other income of all property from time to time subjected to the lien of this Indenture, and all right, title and interest of every nature whatsoever of the Owner Trustee in and to the same and every part thereof; and

(5) all proceeds of the foregoing;

BUT EXCLUDING from the Lease Indenture Estate any and all Excepted Payments and Excepted Rights; and SUBJECT, HOWEVER, TO (i) the terms and provisions of this Indenture and (ii) the rights of the Lessee under the Facility Lease.

To the extent that any portion of the Lease Indenture Estate constitutes fixtures or real property, this Indenture constitutes a realty mortgage and an assignment of rents with respect to all such items of real property and, in addition to all other rights or remedies set forth in this Indenture, the Indenture Trustee shall have, to the extent not inconsistent with this Indenture, all of the rights, remedies and benefits of a mortgagee of real property under Applicable Law, including, without limitation, the rights and remedies pursuant to Arizona Revised Statutes, Section 33-702.B, and the Owner Trustee shall be deemed a mortgagor with respect to such items.

Concurrently with the delivery hereof, the Owner Trustee is delivering to the Indenture Trustee the executed original counterpart of the Facility Lease and the Assignment and Assumption (which the Indenture Trustee will at all times maintain possession of).

TO HAVE AND TO HOLD all the Lease Indenture Estate unto the Indenture Trustee, its successors and

assigns FOREVER, BUT IN TRUST, NEVERTHELESS, for the ratable benefit and security of the Holders of the Notes without priority of any one Note over the other except as herein otherwise expressly provided, and for the uses and purposes and subject to the terms and conditions set forth in this Indenture.

UPON CONDITION that, unless and until an Indenture Event of Default shall have occurred and be continuing, the Owner Trustee shall be permitted, to the exclusion of the Indenture Trustee, but subject to the provisions hereof, including, without limitation, Sections 6.11 and 10.2, to possess and use the Lease Indenture Estate and exercise all rights with respect thereto and, without limitation of the foregoing, the Owner Trustee may exercise all of its rights under the Granting Clause Documents to the same extent as if its right, title and interest therein had not been assigned to the Indenture Trustee, except that the Indenture Trustee shall receive all payments of Assigned Payments and all moneys and securities required to be held by or deposited with the Indenture Trustee hereunder.

It is expressly agreed that, anything herein contained to the contrary notwithstanding, the Owner Trustee shall remain obligated under the Granting Clause Documents to perform all of the Owner Trustee's obligations thereunder in accordance with the terms and provisions thereof, and the Indenture Trustee shall not be required or obligated in any manner, except as expressly provided herein, to perform or fulfill any obligations of the Owner Trustee under any Granting Clause Document or to make any payment, or to make any inquiry as to the nature or sufficiency of any payment received by it, or to present or file any claim, or to take any action to collect or enforce the payment of any amounts or otherwise to protect or preserve any rights which may have been assigned to it or to which it may be entitled at any time or times.

The Owner Trustee hereby warrants and represents that it has not assigned or pledged any of its right, title or interest in and to the Lease Indenture Estate to anyone other than the Indenture Trustee or otherwise granted or created any right prior to or inconsistent with the rights of the Indenture Trustee under this Indenture.

SECTION 2.2. Payments Under Granting Clause Documents.

Until release of the lien of the Lease Indenture Estate, all payments due or to become due under any Granting Clause Document to the Owner Trustee (except so much of such payments as constitute Excepted Payments) shall be made directly to the Indenture Trustee or in accordance with the Indenture Trustee's instructions. The Owner Trustee agrees that if it should receive any such payments to be made to the Indenture Trustee or any proceeds for or with respect to the Lease Indenture Estate or as a result of the sale or other disposition thereof or otherwise constituting part of the Lease Indenture Estate to which the Owner Trustee is not entitled hereunder, it will promptly forward such payments to the Indenture Trustee or in accordance with the Indenture Trustee's instructions. The Indenture Trustee agrees to apply payments from time to time received by it (from the Lessee, the Owner Trustee or otherwise) with respect to the Lease Indenture Estate in the manner provided in Section 3.11 and Article V.

SECTION 2.3. Release of Security Interest in Undivided Interest and Real Property Interest.

In case a release from the security and other interests created by Section 2.1 by the Indenture Trustee of a portion of the Lease Indenture Estate shall be necessary in order to enable the Lessee to perform its covenants and agreements set forth in Section 10(b)(2) of the Participation Agreement or the Owner Trustee or the Lessee to carry out any action required by Section 8 of the Facility Lease, the Indenture Trustee shall execute and deliver to, or as directed by, the Owner Trustee an appropriate instrument or instruments provided to the Indenture Trustee by the Owner Trustee or the Lessee (in due form for filing or recording), so releasing a portion of the Lease Indenture Estate from said Lien provided that the Indenture Trustee shall have first received a certificate in form and substance reasonably satisfactory to the Indenture Trustee, executed by the Lessee or the Owner Trustee, accompanied by an opinion of counsel reasonably satisfactory to the Indenture Trustee, each of which shall be to the effect that all necessary actions have been or are being taken simultaneously with such release in connection with the proposed action to comply with the terms of this Indenture and the relevant Transaction Documents and that, in the case of releases

required by Section 8(c) of the Facility Lease, all documents necessary to perfect, protect and preserve the lien created by this Indenture with respect to the Capital Improvements which are to be subjected to the lien of this Indenture have been duly authorized and properly executed and have been delivered to the Indenture Trustee, it being understood that insofar as such certificate and opinion relates to the due authority of, and proper execution of documents by, the Owner Trustee, the Lessee and the Indenture Trustee may rely upon a certificate of, and accompanying opinion of counsel to, the Owner Trustee. Notwithstanding the foregoing, (i) no opinion of counsel need be delivered with respect to the release by the Indenture Trustee of security with an aggregate value of less than \$500,000 unless specifically requested by the Indenture Trustee, provided such proposed action complies with the terms of the Facility Lease, and (ii) to the extent that the Lessee and the Owner Trustee shall mutually agree on, and shall deliver a certificate to the Indenture Trustee evidencing such agreement with respect to, a new arrangement relating to the Real Property Interest, the Indenture Trustee shall take all actions mutually requested by the Owner Trustee and the Lessee set forth in such certificate.

SECTION 2.4. Release of Lien on Lease Indenture Estate.

(a) Upon the Indenture Trustee's determination, evidenced by its certificate delivered to (1) during the period that any Initial Series Notes are Outstanding, the Agent, (2) during the period that Funding Corp is the Holder of the Notes, the Collateral Trust Trustee, or (3) at all other times, the Holders of the Outstanding Notes, that (i) it has received, or provision has been made in accordance with paragraph (c) of this Section 2.4 for, full payment of all principal of and premium, if any, and interest on the Notes and any other sums payable to the Indenture Trustee and the Holders of the Notes under this Indenture, the Notes and any of the Granting Clause Documents, and (ii) all Trustee's Expenses shall have been paid in full or provision satisfactory to the Indenture Trustee shall have been made for such payment,

(A) the lien and all other estate and rights granted by this Indenture shall cease, determine and terminate and all of the property, rights and interests included in the Lease Indenture Estate

shall revert to and revest in the Owner Trustee without any other act or formality whatsoever, and

(B) the Indenture Trustee shall, at the request of the Owner Trustee, execute and deliver to the Owner Trustee such termination statements, releases or other instruments presented to the Indenture Trustee by or at the direction of the Owner Trustee as shall be requisite to evidence the satisfaction and discharge of this Indenture and the lien hereby created with respect to the Lease Indenture Estate, to release or reconvey to the Owner Trustee or as directed by the Owner Trustee all the Lease Indenture Estate, freed and discharged from the provisions herein contained with respect thereto, and to release the Owner Trustee from its covenants herein contained.

(b) Upon satisfaction of the conditions, and receipt by the Indenture Trustee of the Assumption Agreement and other documents and opinions, described in Section 3.9(b), the Indenture Trustee shall, at the request of the Owner Trustee, execute and deliver to the Owner Trustee such agreements, releases or other instruments presented to the Indenture Trustee by or at the direction of the Owner Trustee as shall be requisite to evidence the satisfaction and discharge of this Indenture as to the Owner Trustee and to release the Owner Trustee from its covenants herein contained. The satisfaction and discharge of this Indenture as to the Owner Trustee shall not operate as a satisfaction and discharge of the lien created hereby with respect to the Lease Indenture Estate notwithstanding the fact that the Facility Lease may have terminated as a matter of law and that, as a consequence, any rights of the Owner Trustee under the ANPP Participation Agreement and the Assignment and Assumption may no longer exist.

(c) Any Note, other than any of the Initial Series Notes, shall, prior to the maturity or redemption date thereof, be deemed to have been paid within the meaning and with the effect expressed in this Section 2.4(c) if (i) there shall have been deposited with the Indenture Trustee either moneys in an amount which shall be sufficient, or direct obligations of or obligations the principal of and interest on which are unconditionally guaranteed by the United States of America or certificates of an ownership interest in the principal of or interest on obligations of or guaranteed as to principal and interest by the United States of

America (Federal Securities), in each case which shall not contain provisions permitting the redemption thereof at the option of the issuer, the principal of and the interest on which when due, and without any reinvestment thereof, will provide moneys in an amount which shall be sufficient, together with the moneys, if any, deposited with or held by the Indenture Trustee at the same time (such sufficiency to be established by the delivery to the Indenture Trustee of a certificate of an independent public accountant), to pay when due the principal of and premium, if any, and interest due and to become due on said Note on and prior to the redemption date or maturity date thereof, as the case may be, and (ii) in the event said Note does not mature or is not to be redeemed within the next 45 days, the Indenture Trustee shall have been given irrevocable instructions to give, as soon as practicable, a notice to the registered Holder of such Note that the deposit required by subclause (i) above has been made with the Indenture Trustee and that said Note is deemed to have been paid in accordance with this Section 2.4(c) and stating such maturity or redemption date upon which moneys are to be available for the payment of the principal of and premium, if any, and interest on said Note. Neither the Federal Securities nor moneys deposited with the Indenture Trustee pursuant to this Section 2.4(c) or principal or interest payments on any such Federal Securities 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 on said Note; provided, however, that any cash received from such principal or interest payments on such Federal Securities deposited with the Indenture Trustee, shall be reinvested pursuant to Section 8.8 in Federal Securities. At such time as any Note shall be deemed paid as aforesaid, it shall no longer be secured by or entitled to the benefits of the Lease Indenture Estate or, except as provided in Section 2.4(d), of this Indenture.

(d) So long as any Note as to which this Indenture has been discharged remains unpaid, this Indenture shall continue in effect with respect to such Note solely with respect to rights of registration of transfer, exchange or replacement of such Note, rights to receive payment of the principal thereof and premium, if any, and interest thereon in accordance with the terms of this Indenture from such deposited funds or the proceeds of or interest on such Federal Securities and the correlative rights and responsibilities of the

Indenture Trustee; provided, however, that, following such discharge, no claim for payment of principal of or premium, if any, or interest on such Note shall be made against the Owner Trustee or the Lease Indenture Estate other than as provided in this Section; provided, further, that the Owner Trustee, following such discharge, shall be released from any further duties or obligations under this Indenture and, except as expressly provided therein, any other Transaction Document.

SECTION 2.5. Severance.

The parties hereto understand and agree and it is their express intention that Unit 2 (including the Undivided Interest), each Capital Improvement and each part thereof is or shall be severed, and shall be and remain severed, from the real estate constituting the PVNGS Site and even if physically attached thereto, shall retain the character of personal property, shall be treated as personal property with respect to the rights of all persons whomsoever, shall not be or become fixtures or otherwise part of the real estate constituting the PVNGS Site, and, by virtue of its nature as personal property, shall not be affected in any way by any instrument dealing with the real estate constituting the PVNGS Site.

SECTION 2.6. Power of Attorney.

Subject to the other terms of this Indenture, the Owner Trustee hereby appoints, effective whenever an Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee the Owner Trustee's attorney-in-fact, irrevocably, with full power of substitution, to collect, ask, require, demand, receive and give acquittance for any and all moneys and claims for moneys due and to become due to the Owner Trustee under or arising out of the Lease Indenture Estate, to endorse any checks or other instruments or orders in connection therewith, and to take any action (including the filing of financing statements or other documents) or institute any proceedings which the Indenture Trustee may deem to be necessary or appropriate to protect and preserve the interest of the Indenture Trustee in the Lease Indenture Estate.

ARTICLE III

ISSUE, EXECUTION, AUTHENTICATION, FORM AND REGISTRATION OF NOTES

SECTION 3.1. Limitation on Notes.

No Notes may be issued under the provisions of, or become secured by, this Indenture except in accordance with the provisions of this Article III. No Note shall be issued in an original principal amount of less than \$150,000.

SECTION 3.2. Execution of Notes.

All Notes shall be manually executed on behalf of the Owner Trustee by one of its Responsible Officers. In case any Responsible Officer of the Owner Trustee who shall have executed any of the Notes shall cease to be such a Responsible Officer before such Notes so executed shall have been authenticated by the Indenture Trustee and delivered or disposed of by the Owner Trustee, such Notes nevertheless may be authenticated and delivered or disposed of as though the person who executed such Notes had not ceased to be such a Responsible Officer of the Owner Trustee; and any Note may be executed on behalf of the Owner Trustee by such person as, at the actual time of execution of such Note, shall be a Responsible Officer of the Owner Trustee, although at the date of such Note any such person was not such a Responsible Officer.

SECTION 3.3. Effect of Certificate of Authentication.

Only such Notes as shall bear thereon a certificate of authentication substantially in the following form manually executed by the Indenture Trustee shall be entitled to the benefits of this Indenture or be valid or obligatory for any purpose. Such certificate of authentication of the Indenture Trustee upon any Note executed by the Owner Trustee shall be conclusive evidence that the Note so authenticated was duly issued, authenticated and delivered under this Indenture:

This Note is one of the series of Notes referred to therein and in the within-mentioned Indenture.

CHEMICAL BANK
as Indenture Trustee,

By _____
Authorized Officer

SECTION 3.4. Creation of the Initial Series Notes; Aggregate Principal Amount, Dating and Terms.

(a) There is hereby created and established a separate series of Notes of the Owner Trustee designated: "Nonrecourse Promissory Note, Initial Series", which shall be substantially in the form of, and shall contain the terms set forth in, Exhibit A hereto, and are herein referred to as the "Initial Series Notes".

(b) The Initial Series Notes shall be executed and issued by the Owner Trustee and authenticated and delivered by the Indenture Trustee on the date and to the Persons specified by the Owner Trustee in its request and authorization for issuance, shall be dated the date specified by the Owner Trustee in its request and authorization for issuance, and shall be in the form of registered Notes registered in the names of the Persons designated in the Owner Trustee's request and authorization for issuance or its registered assigns.

(c) The Initial Series Notes shall bear interest on the principal amount thereof from time to time Outstanding from the date thereof until paid at the rates of interest set forth in the form of the Initial Series Notes. The principal amount of the Initial Series Notes shall be payable as set forth in the Schedule of Principal Payments attached thereto. Interest on the Initial Series Notes shall be due and payable at the times specified in the form of Initial Series Notes.

SECTION 3.5. Additional Notes.

(1) Subject to Section 3.6, and upon condition that (A) no Default or Event of Default or Indenture Event of Default has occurred and is continuing and (B) payments pursuant to the Facility Lease of Basic Rent, Casualty Value, Special Casualty Value and of amounts in respect of the Cure Option are sufficient to pay as and when due all amounts of principal of and premium, if any, and interest on all Outstanding Notes, after taking into account the issuance of such Additional Notes and any related redemption, Additional Notes of the Owner Trustee may be issued under and secured by this Indenture, at any time or from time to time, in addition to the Initial Series Notes and subject to the conditions hereinafter provided in this Section, for cash in the amount of the original principal amount of such Additional Notes, but only for the purpose of (i) refunding any previously issued series of Notes, in whole or in part and/or (ii) providing funds for the payment of all or any portion of the Supplemental Financing Amount relating to Capital Improvements made or installed from time to time pursuant to the Facility Lease and/or (iii) providing funds to be paid to the Owner Trustee in the event of a partial return of the Investment to the Owner Trustee as contemplated by Section 2(d) or 2(e) of the Participation Agreement; provided, however, that (x) in the case of Notes issued for the purposes set forth in clause (ii) or (iii) of this Section 3.5, no Note shall be issued by the Owner Trustee pursuant to this Section 3.5 unless such Notes may be pledged in accordance with the Collateral Trust Indenture and serve as the basis for Additional Bonds and (y) in the case of Notes issued for the purposes set forth in clause (i) or (iii) of this Section 3.5, no Note shall be issued by the Owner Trustee pursuant to this Section 3.5 unless Section 2(d) and/or 2(e) of the Participation Agreement (if applicable) shall have been complied with and provided, further that so long as any Initial Series Notes are Outstanding, Additional Notes may be issued only if all principal of, and premium, if any, and accrued interest on, all such Initial Series Notes are simultaneously paid in full.

(2) Before any Additional Notes shall be issued under the provisions of this Section 3.5, the Owner Trustee shall have received from the Equity Participant, and delivered to the Indenture Trustee not less than 10 nor more than 30 days prior to the proposed

date of issuance of such Additional Notes as set forth in the below-mentioned request and authorization, a request and authorization to issue Additional Notes, which request and authorization shall include the amount of such Additional Notes, the date of issuance of such Additional Notes and details with respect thereto which are not inconsistent with this Section. Additional Notes shall have a designation so as to distinguish each Series of Additional Notes from each other series of Additional Notes but otherwise each such series shall be substantially similar in terms to each other such series, shall specify maturity dates, rank pari passu with all Notes then Outstanding, be dated their respective dates of authentication, bear interest at such rates (which may be fixed or floating) as shall be indicated in the aforementioned request and authorization, and shall be stated to be payable by their terms not later than the last day of the Basic Lease Term.

(3) Except as to any differences in the maturity dates and amortization schedules of the Additional Notes or the rate or rates of interest thereon and the date or dates such interest is payable or the provisions for redemption with respect thereto, if any, such Additional Notes shall be on a parity with, and shall be entitled to the same benefits and security of this Indenture as, other Notes issued pursuant to the terms hereof.

(4) The terms, conditions and designations of such Additional Notes (which shall be consistent with this Indenture) shall be set forth in an indenture supplemental to this Indenture executed by the Owner Trustee and the Indenture Trustee. Such Additional Notes shall be executed as provided in Section 3.2 and deposited with the Indenture Trustee for authentication, but before such Additional Notes shall be authenticated and delivered by the Indenture Trustee there shall be filed with the Indenture Trustee, in addition to the other documents and certificates required by this Section 3.5, the following, all of which shall be dated as of the date of the supplemental indenture:

(a) a copy of such supplemental indenture (which shall include the form of such series of Notes in respect thereof);

(b) a certificate of a Responsible Officer of the Owner Trustee (i) stating that to the best of his knowledge, no Default or Event of Default or Indenture

Event of Default has occurred and is continuing, (ii) stating that the conditions in respect of the issuance of such Additional Notes contained in this Section 3.5 have been satisfied, (iii) specifying the amount of the costs and expenses relating to the issuance and sale of such Additional Notes, (iv) stating that payments pursuant to the Facility Lease of Basic Rent, Casualty Value and Special Casualty Value and of amounts in respect of the exercise of the Cure Option are sufficient to pay as and when due all amounts of principal of and premium, if any, and interest on all the Outstanding Notes; after taking into account the issuance of such Additional Notes and any related redemption, and (v) in the case of Notes issued for the purpose set forth in clause (ii) of Section 3.5(1), stating that, to the best of his knowledge, all conditions to the related Supplemental Financing as set forth in Section 8(f) of the Facility Lease have been satisfied or waived in accordance with such Section 8(f);

(c) such additional documents, certificates and opinions as shall be reasonably requested by, and acceptable to, the Owner Trustee and the Indenture Trustee;

(d) a request and authorization to the Indenture Trustee by or on behalf of the Owner Trustee to authenticate and deliver such Additional Notes to or upon the order of the Person or Persons noted in such request at the address set forth therein, and in such principal amounts as are stated therein, upon payment to the Indenture Trustee, but for the account of the Owner Trustee, of the sum or sums specified in such request and authorization; and

(e) an opinion of counsel to the effect that the conditions precedent required under this Indenture for the issuance of such Additional Notes have been complied with.

When the documents referred to in the foregoing clauses (a) through (e) above shall have been filed with the Indenture Trustee and when the Additional Notes described in the above-mentioned request and authorization shall have been executed and authenticated as required by this Indenture, the Indenture Trustee shall deliver such Additional Notes in the manner described in clause (d) above, but only upon payment to the Indenture Trustee of the sum or sums specified in such request and authorization.

SECTION 3.6. Security for and Parity of Notes.

All Notes issued and Outstanding hereunder shall rank on a parity with each other and shall as to each other be secured equally and ratably by this Indenture, without preference, priority or distinction of any thereof over any other by reason of difference in time of issuance or otherwise.

SECTION 3.7. Source of Payments Limited.

All payments to be made by the Owner Trustee under this Indenture or on the Notes shall be made only from the Lease Indenture Estate and the Trust Estate. Each Holder of a Note, by its acceptance of such Note, and the Indenture Trustee agree that they will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to such Holder or the Indenture Trustee as herein provided and that neither the Equity Participant nor, except as expressly provided in this Indenture, the Owner Trustee nor the Indenture Trustee, shall be personally liable to such Holder of a Note or the Indenture Trustee, as the case may be, for any amounts payable hereunder or under such Note; provided, however, that in the event, and to the extent, that the Lessee shall assume all the obligations and liabilities of the Owner Trustee hereunder and under the Notes pursuant to Section 3.9(b), then all payments to be made under this Indenture and the Notes shall be made only from payments made by the Lessee under the Notes in accordance with the Assumption Agreement referred to in Section 3.9(b) and, subject to Section 2.4 hereof, from the Lease Indenture Estate and each Holder of a Note and the Indenture Trustee agree that in such event they will look solely to the Lessee and the Lease Indenture Estate for such payment. Nothing herein contained shall be interpreted as affecting the duties and obligations of the Indenture Trustee set forth in Section 7.4.

In furtherance of the foregoing, to the fullest extent permitted by law, each Holder of a Note (and each assignee of such Person), by its acceptance thereof, and the Indenture Trustee agree, as a condition to the Notes being secured under this Indenture, that neither such Holder nor the Indenture Trustee will exercise any statutory right to negate the agreements set forth in this Section 3.7.

SECTION 3.8. Place and Medium of Payment.

The principal of and premium, if any, and interest on each Note shall be payable at the Indenture Trustee's Office in immediately available funds 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. Notwithstanding the foregoing or any provision in any Note to the contrary, if so requested by the Holder of any Note, by written notice to the Indenture Trustee, all amounts (other than the final payment) payable with respect to such obligation shall be paid by crediting the amount to be distributed to such Holder to an account maintained by such Holder with the Indenture Trustee or by the Indenture Trustee's transferring such amount by wire, with such wire transfer to be initiated by such time as to permit, to the extent practicable, oral confirmation thereof (specifying the wire number) to be given no later than 1:00 P.M. New York City time on the date scheduled for payment, but only to the extent of funds available for such wire transfer, to such other bank in the United States having wire transfer facilities, including a Federal Reserve Bank, as shall have been specified in such notice, for credit to the account of such Holder maintained at such bank, any such credit or transfer pursuant to this Section 3.8 to be in immediately available funds, without any presentment or surrender of such Note. Final payment of any such Note shall be made only against surrender of such Note at the Indenture Trustee's Office.

SECTION 3.9. Prepayment of Notes; Assumption by Lessee; Notice of Assumption or Prepayment.

(a) Notes shall be subject to prepayment (other than through application of the installment payments on such Notes) from time to time only as provided in this Indenture and as otherwise specifically provided, with respect to Notes of a particular series, in such Notes.

(b) In the event of the occurrence of a Deemed Loss Event or Event of Loss or exercise of the Cure Option, and upon receipt by the Indenture Trustee of the documents listed below, (i) all the obligations and liabilities of the Owner Trustee hereunder and under the Notes shall be assumed by the Lessee, (ii) if any Initial Series Notes are Outstanding, the Lessee shall assume all obligations and liabilities of the Owner

Trustee thereunder pursuant to agreements substantially in the form of, and containing the terms set forth in, Exhibit C hereto (such Initial Series Notes when assumed pursuant to such agreements are herein referred to as the Bank Exchange Notes), and (iii) the Owner Trustee shall be released and discharged without further act or formality whatsoever from all obligations and liabilities hereunder and under the Notes:

(1) a duly executed Assumption Agreement substantially in the form of Exhibit B hereto;

(2) an opinion of counsel, addressed to the Indenture Trustee and the Holders of the Outstanding Notes, to the effect that the conditions precedent required by this Indenture for such assumption have been complied with, that the Assumption Agreement has been duly authorized, executed and delivered on behalf of the Lessee, that no Governmental Action is necessary or required in connection therewith (or if any such Governmental Action is necessary or required, that the same has been duly obtained and is in full force and effect), and that the Assumption Agreement is a legal, valid and binding agreement and obligation of the Lessee, enforceable in accordance with its terms (except as limited by bankruptcy, insolvency or similar laws of general application affecting the enforcement of creditors' rights generally and equitable principles);

(3) copies of all Governmental Actions referred to in such opinion;

(4) an indenture supplemental to this Indenture which shall, among other things, confirm the release of the Owner Trustee thereby effected and may contain provisions appropriately amending references to the Facility Lease in this Indenture;

(5) a certificate of a Responsible Officer of the Lessee stating that (i) the conditions precedent required by this Indenture for such assumption have been complied with, (ii) such assumption is permitted by the provisions of the Lessee's Restated Articles of Incorporation and By-Laws and has been authorized by all requisite corporate action, and (iii) the Lessee is not insolvent within the meaning of any applicable preferential

transfer, fraudulent conveyance or bankruptcy law; and

(6) if Initial Series Notes are to be exchanged for Bank Exchange Notes, at the request of the Holders of the Initial Series Notes, an Assignment, Assumption and Further Agreement between the Lessee and the Indenture Trustee substantially in the form of the Assignment and Assumption, with such changes, if any, as the Indenture Trustee shall reasonably request to enable the Holders of the Notes to benefit from their security interest in the Lease Indenture Estate.

(c) Notice of any assumption or prepayment of Notes shall be given to the registered Holders of the Notes which have been assumed or are to be prepaid (and any assignee of a registered Holder which has given the Indenture Trustee written notice of such assignment) as promptly as practicable after the Indenture Trustee is notified thereof, and, in the case of prepayment, in no event less than 30 days before the date fixed for prepayment (provided the Indenture Trustee receives such notification at least three Business Days before such 30th day), in the event of the exercise by the Lessee or the Owner Trustee, as the case may be, of its option to terminate the Facility Lease pursuant to Section 14 thereof or in the event of the exercise by the Lessee of the Cure Option.

SECTION 3.10. Mutilated, Destroyed, Lost or Stolen Notes.

If any Note shall become mutilated or shall be destroyed, lost or stolen, the Owner Trustee shall, upon the written request of the Holder of such Note, execute, and the Indenture Trustee shall authenticate and deliver in replacement thereof, a new Note, payable in the same original principal amount and dated the same date and of the same series as the Note so mutilated, destroyed, lost or stolen. The Indenture Trustee shall make a notation on each new Note of the amount of all payments of principal theretofore made on the Note so mutilated, destroyed, lost or stolen and the date to which interest on such old Note has been paid. If the Note being replaced has been mutilated, such Note shall be delivered to the Indenture Trustee who shall then deliver a certificate of destruction of the type required by Section 4.3. If the Note being replaced has been destroyed, lost or stolen, the Holder of such Note shall furnish to the Lessee, the Owner Trustee and the

Indenture Trustee a bond or surety agreement of such Holder as shall be satisfactory to them to save the Lessee, the Owner Trustee, the Indenture Trustee, the Trust Estate and the Lease Indenture Estate harmless from any loss, however remote, including claims for principal of, and premium, if any, and interest on the purportedly destroyed, lost or stolen Note, together with evidence satisfactory to the Lessee, the Owner Trustee and the Indenture Trustee of the destruction, loss or theft of such Note and of the ownership thereof; provided, however, that if the Holder of such Note is the Collateral Trust Trustee, the unsecured written undertaking of the Collateral Trust Trustee, in its individual capacity, shall be sufficient indemnity for purposes of this Section.

SECTION 3.11. Allocation of Principal and Interest.

In the case of each Note, each payment of principal thereof and interest thereon shall be applied, first, to the payment of accrued but unpaid interest on such Note (as well as any interest on overdue principal or, to the extent permitted by law, interest) to the date of such payment, second, to the payment of the principal amount of, and premium, if any, on such Note then due (including any overdue installment of principal) thereunder and third, the balance, if any, remaining thereafter, to the balance of the payment of the principal amount of, and premium, if any, on such Note.

SECTION 3.12. Certain Adjustments to Amortization Schedules of Notes.

The schedules of principal amortization attached to the Outstanding Refunding Notes may be adjusted at the discretion of the Owner Trustee at one time prior to June 30, 1989; provided, however, such adjustment only may be made in connection with an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease. If the Owner Trustee shall elect to make the foregoing adjustment, the Owner Trustee shall deliver to the Indenture Trustee and to the Lessee at least 60 days prior to the first payment date (specified on the schedules hereto) proposed to be affected by such adjustment, a certificate of the Owner Trustee (x) stating that the Owner Trustee has elected to make such adjustment, (y) setting forth the revised schedules of principal amortization for each of the Outstanding Refunding Notes and (z) attaching calculations showing that the average life of the Outstanding Refunding Notes

will not be reduced or increased except as permitted by this Section 3.12. The Indenture Trustee may rely on such Owner Trustee certificate and shall have no duty with respect to the calculations referred to in the foregoing clause (z).

ARTICLE IV

REGISTRATION, TRANSFER, EXCHANGE, CANCELLATION AND OWNERSHIP OF NOTES

SECTION 4.1. Register of Notes.

The Indenture Trustee on behalf of the Owner Trustee shall maintain at the Indenture Trustee's Office a register for the purpose of registration, and registration of transfer and exchange, of the Notes by series and in which shall be entered the names and addresses of the owners of such Notes and the principal amounts of the Notes owned by them, respectively. For these purposes, the Indenture Trustee is hereby appointed transfer agent and registrar for the Notes.

SECTION 4.2. Registration of Transfer or Exchange of Notes.

A Holder of a Note intending to register the transfer of any Outstanding Note held by such Holder (including any transfer in the form of a pledge or assignment) or to exchange any Outstanding Note held by such Holder for a new Note or Notes of the same series may surrender such Outstanding Note at the Indenture Trustee's Office, together with the written request of such Holder, or of its attorney duly authorized in writing, in each case with signatures guaranteed, for the registration of such Note in the name of any pledgee or assignee (in the case of a transfer in the form of a pledge or assignment) or for the issuance of a new Note or Notes of the same series, specifying the authorized denomination or denominations of any new Note or Notes to be issued and the name and address of the Person or Persons in whose name or names the Note or Notes are to be registered (either as pledgee or assignee or as owner). Promptly upon receipt by the Indenture Trustee of the foregoing and satisfaction of the requirements of Sections 4.5 and 4.6, the Indenture Trustee shall

register such Note or Notes in the name or names of the Person or Persons as shall be specified in the written request and, in the case in which a new Note or Notes are to be issued, the Owner Trustee shall execute and the Indenture Trustee shall authenticate and deliver such new Note or Notes of the same series, in the same aggregate principal amount and dated the same date as the Outstanding Note surrendered, in such authorized denomination or denominations as shall be specified in the written request. The Indenture Trustee shall make a notation on each new Note of the amount of all payments of principal theretofore made on the old Note or Notes in exchange or transfer for which any new Note has been issued and the date to which interest on such old Note or Notes has been paid.

SECTION 4.3. Cancellation of Notes.

All Notes surrendered to the Indenture Trustee for payment in full, prepayment in full or registration of transfer or exchange shall be cancelled by it; and no Notes shall be issued in lieu thereof except as expressly permitted by this Indenture. The Indenture Trustee shall destroy cancelled Notes held by it in a manner satisfactory to the Owner Trustee and deliver a certificate of destruction to the Owner Trustee. If the Owner Trustee shall acquire any of the Notes, such acquisition shall not operate as a redemption of or the satisfaction of the indebtedness represented by such Notes unless and until the same shall be delivered to the Indenture Trustee for cancellation.

SECTION 4.4. Limitation on Timing of Registration of Notes.

The Indenture Trustee shall not be required to register transfers or exchanges of Notes on any date fixed for the payment or prepayment of principal of or interest on the Notes or during the fifteen days preceding any such date.

SECTION 4.5. Restrictions on Transfer Resulting from Federal Securities Laws; Legend.

If not prohibited by the Securities Act, each Note shall be delivered to the initial Holder thereof without registration of such Note under the Securities Act and without qualification of this Indenture under the Trust Indenture Act. Prior to any transfer of any Note, in whole or in part, to any Person other than the

Collateral Trust Trustee, the Holder thereof shall furnish to the Lessee, the Indenture Trustee and the Owner Trustee an opinion of counsel, which opinion and which counsel shall be reasonably satisfactory to the Indenture Trustee, the Owner Trustee and the Lessee, to the effect that such transfer will not violate the registration provisions of the Securities Act or require qualification of this Indenture under the Trust Indenture Act, and all Notes issued hereunder shall be endorsed with a legend which shall read substantially as follows:

This Note has not been registered under the Securities Act of 1933 and may not be transferred, sold or offered for sale in violation of such Act.

SECTION 4.6. Charges upon Transfer or Exchange of Notes.

As a further condition to registration of transfer or exchange of any Note, the Indenture Trustee and the Owner Trustee may charge the Holder thereof for any stamp taxes or governmental charges required to be paid with respect to such registration of transfer or exchange.

SECTION 4.7. Inspection of Register of Notes.

The register of the Holders of the Notes referred to in Section 4.1 shall at all reasonable times be open for inspection by any Holder of a Note. Upon request by any Holder of a Note, or the Owner Trustee or the Lessee, the Indenture Trustee shall furnish such Person, at the expense of such Person, with a list of the names and addresses of all Holders of Notes entered on the register kept by the Indenture Trustee indicating the series, principal amount and number of each Note held by each such Holder.

SECTION 4.8. Ownership of Notes.

(a) Prior to due presentment for registration of transfer of any Note, the Owner Trustee and the Indenture Trustee may deem and treat the Holder of record of such Note as the absolute owner of such Note for the purpose of receiving payment of all amounts payable with respect to such Note and for all other purposes, and neither the Owner Trustee nor the

Indenture Trustee shall be affected by any notice to the contrary.

(b) The Owner Trustee and the Indenture Trustee may, in their discretion, treat the Holder of record of any Note as the owner thereof without actual production of such Note for any purpose hereunder, except as provided in the last sentence of Section 3.8.

(c) Neither the Owner Trustee nor the Indenture Trustee shall be bound to take notice of or carry out the execution of any trust in respect of any Note, and may register the transfer of the same on the direction of the Holder of record thereof, whether named as trustee or otherwise, as though such Holder were the beneficial owner thereof.

(d) The receipt by the Holder of record of any Note of any payment of principal, premium or interest shall be a good discharge to the Owner Trustee and the Indenture Trustee for the same and neither the Owner Trustee nor the Indenture Trustee shall be bound to inquire into the title of any such Holder.

ARTICLE V

RECEIPT, DISTRIBUTION AND APPLICATION OF INCOME AND PROCEEDS FROM THE LEASE INDENTURE ESTATE

SECTION 5.1. Basic Rent and Interest on Overdue Installments of Basic Rent.

Except as otherwise provided in Section 5.3 or 5.7, each payment of Basic Rent, as well as any payment of Supplemental Rent representing interest on overdue installments of Basic Rent, received by the Indenture Trustee at any time, shall be distributed by the Indenture Trustee in the following order of priority: first, so much of such payment as shall be required to pay in full the aggregate amount of the payment or payments of principal and premium, if any, and/or interest (as well as any interest on overdue principal or, to the extent permitted by law, interest) then due and unpaid on all Notes shall be distributed to the Holders of the Notes ratably, without priority of one over the other, in the proportion that the aggregate amount of such

payment or payments then due and unpaid on all Notes held by each such Holder on such date bears to the aggregate amount of such payment or payments then due and unpaid on all Notes Outstanding on such date, without priority of interest over principal or principal over interest; and second, the balance, if any, of such payment remaining thereafter shall be distributed, concurrently with any distribution pursuant to clause first hereof, to the Owner Trustee or as the Owner Trustee may direct. If there shall not otherwise have been distributed on any date (or within any applicable period of grace), pursuant to this Section 5.1, the full amount then distributable pursuant to clause first of this Section 5.1, the Indenture Trustee shall distribute other payments of the character referred to in Sections 5.4 and 5.5 then held by it or thereafter received by it, except as otherwise provided in Section 5.3, to the Holders of all Notes to the extent necessary to enable it to make all the distributions then due pursuant to such clause first; provided that to the extent any distribution is made from amounts held pursuant to Section 5.4 and the Lessee subsequently makes the payment of Basic Rent or Supplemental Rent in respect of which such distribution was made, such payment of Basic Rent or Supplemental Rent shall, unless a Default or an Event of Default shall have occurred and be continuing, be applied to the purpose for which such amount held pursuant to Section 5.4 had been held, subject, in all cases, to the terms of Section 5.4. The portion of each such payment made to the Indenture Trustee which is to be distributed by the Indenture Trustee in payment of Notes shall be applied in accordance with Section 3.11. Any payment received by the Indenture Trustee pursuant to Section 6.8 shall be distributed to the Holders of the Notes, ratably, without priority of one over the other, in the proportion that the amount of such payment or payments then due and unpaid on all Notes held by each such Holder bears to the aggregate amount of the payments then due and unpaid on all Notes Outstanding. Amounts distributed by the Indenture Trustee pursuant to this Section 5.1 shall be distributed as promptly as practicable after such amounts are actually received by the Indenture Trustee; in the event the Indenture Trustee shall be directed to make payments to the Holder of any Note by wire transfer in accordance with Section 3.8, any amounts received by the Indenture Trustee after 1:00 P.M., New York City time, may be so distributed on the following Business Day.

SECTION 5.2. Amounts Received as Result of Event of Loss, Deemed Loss Event, Exercise of Option to Terminate or Exercise of Cure Option.

If an Event of Loss or Deemed Loss Event shall occur or the Lessee shall exercise the Cure Option, any amounts of Casualty Value, Special Casualty Value or Fair Market Sales Value received or held by the Indenture Trustee in respect of such Event of Loss or Deemed Loss Event or exercise of the Cure Option shall, except as otherwise provided in Section 5.3 be distributed forthwith to the Equity Participant. If the Lessee or Owner Trustee, as the case may be, shall exercise its option to terminate the Facility Lease pursuant to Section 14 thereof, then there shall be prepaid, on the date payments or proceeds with respect thereto are received by the Indenture Trustee (or as soon thereafter as practicable) under Section 14 of the Facility Lease, the unpaid principal amount of all Notes, together with the premium, if any, and all accrued but unpaid interest thereon to the date of such prepayment. Notice of such prepayment shall be given as provided in Section 3.9(c) and may provide that it is subject to receipt of funds for such prepayment. Except as otherwise provided in Section 5.3 or 5.7, any payments received and amounts realized by the Indenture Trustee upon exercise of the Lessee's or the Owner Trustee's option to terminate the Facility Lease under Section 14 thereof shall in each case be distributed on the date of prepayment as provided in clauses first, second and fifth of Section 5.3.

SECTION 5.3. Amounts Received After, or Held at Time of, Indenture Event of Default under Section 6.2.

Except as otherwise provided in Section 5.7, all payments received and amounts realized by the Indenture Trustee in respect of the Lease Indenture Estate (including any amounts realized by the Indenture Trustee from the exercise of any remedies pursuant to the Facility Lease or Article VI of this Indenture) after an Indenture Event of Default referred to in Section 6.2 shall have occurred and be continuing and the Notes have been accelerated pursuant to Section 7.1, as well as all payments thereafter received or amounts then held by the Indenture Trustee as part of the Lease Indenture Estate, shall be distributed by the Indenture Trustee in the following order of priority:

first, so much of such payments or amounts as shall be required to reimburse the Indenture Trustee for any Trustee's Expenses (to the extent not previously reimbursed) and to pay the reasonable remuneration of the Indenture Trustee, shall be applied by the Indenture Trustee to such reimbursement and payment;

second, so much of such payments or amounts remaining as shall be required to pay in full the aggregate unpaid principal amount of all Notes, together with premium, if any, plus accrued but unpaid interest (as well as interest on overdue principal and, to the extent permitted by law, on overdue interest and any other amounts owing thereunder) thereon to the date of distribution, shall be distributed to the Holders of such Notes and in case the aggregate amount so to be distributed shall be insufficient to pay all such Notes in full as aforesaid, then ratably, without priority of one over the other, in the proportion that the aggregate unpaid principal amount of all such Notes held by each such Holder, together with premium, if any, plus accrued but unpaid interest thereon to the date of distribution bears to the aggregate unpaid principal amount of all Notes, together with premium, if any, plus accrued but unpaid interest thereon to the date of distribution;

third, so much of such payments or amounts remaining as shall be required to pay the present or former Holders of the Notes the amounts payable to them as Indemnitees (to the extent not previously reimbursed) shall be distributed to such Holders; and in case the aggregate amount so to be paid to all such Holders in accordance with this clause third shall be insufficient to pay all such amounts as aforesaid, then ratably, without priority of one over the other, in the proportion that the amount of such indemnity or other payments to which such Person is entitled bears to the aggregate amount of such indemnity or other payments to which all such Persons are entitled;

fourth, the balance, if any, of such payments or amounts remaining shall be applied to the payment of any other indebtedness at the time due and owing to the Indenture Trustee or the Holders of the Notes which this Indenture by its terms secures; and

fifth, the balance, if any, of such payments or amounts remaining thereafter shall be distributed to or upon the direction of the Owner Trustee.

SECTION 5.4. Amounts Received for Which Provision Is Made in a Transaction Document.

Except as otherwise provided in Section 5.1, 5.2, 5.3 or 5.7, any payments received by the Indenture Trustee in respect of the Lease Indenture Estate for which provision as to the application thereof is made in a Transaction Document shall be applied to the purpose for which such payment was made in accordance with the terms of such Transaction Document, as determined from instructions or other information accompanying such payment.

SECTION 5.5. Amounts Received for Which No Provision Is Made.

Except as otherwise provided in Section 5.1, 5.2, 5.3 or 5.7, any payments received and any amounts realized by the Indenture Trustee in respect of the Lease Indenture Estate (a) for which no provision as to the application thereof is made in a Transaction Document or elsewhere in this Article V shall be held by the Indenture Trustee as part of the Lease Indenture Estate, and (b) to the extent received or realized at any time after payment in full of the principal of and premium, if any, and interest on all the Notes, as well as any other amounts remaining as part of the Lease Indenture Estate after payment in full of the principal of and premium, if any, and interest on all the Notes, shall be distributed by the Indenture Trustee in the order of priority set forth in Section 5.3 (omitting clause second thereof).

SECTION 5.6. Payments to Owner Trustee.

Unless otherwise directed by the Owner Trustee, all payments to be made to the Owner Trustee hereunder shall be made to the Equity Participant by wire transfer of immediately available funds as soon as practicable but in any event no later than the close of business on the date of receipt (assuming the Indenture Trustee has received such funds prior to 3:00 P.M., New York City time, on the same day) to such account at such bank or trust company as the Equity Participant shall from time to time designate in writing to the Indenture Trustee.

SECTION 5.7. Excepted Payments.

Anything in this Article V or elsewhere in this Indenture to the contrary notwithstanding, any Excepted Payment received at any time by the Indenture Trustee shall be distributed as promptly as practicable to the Person entitled to receive such Payment.

ARTICLE VI

REPRESENTATIONS, WARRANTIES AND COVENANTS OF OWNER TRUSTEE; EVENTS OF DEFAULT; REMEDIES OF THE INDENTURE TRUSTEE

SECTION 6.1. Representations, Warranties and Covenants of Owner Trustee.

The Owner Trustee hereby covenants and agrees that (i) it will duly and punctually pay the principal of, and premium, if any, and interest on, the Notes in accordance with the terms thereof and this Indenture, (ii) it will not create or permit to exist and will promptly discharge any Lessor's Liens, (iii) so long as this Indenture shall remain in effect, it will not purchase or agree to purchase any property or asset other than the Undivided Interest and the Real Property Interest and other than as contemplated by the Transaction Documents, (iv) it will not, except with the prior written concurrence of the Indenture Trustee or as expressly provided in or permitted by this Indenture or with respect to the Trust Agreement or any property not constituting part of the Lease Indenture Estate, take any action which would result in an impairment of any Note or the obligation of the Lessee to pay any amount under the Facility Lease which is part of the Lease Indenture Estate (not in any event including in respect of Excepted Payments and Excepted Rights) or any of the other rights or security created or effected thereby, except as contemplated by the Transaction Documents, or (v) it will not issue, or incur any obligation in respect of, indebtedness for borrowed money except for its obligations in respect of Notes.

A signed copy of any amendment or supplement to the Trust Agreement shall be delivered by the Owner Trustee to the Indenture Trustee and the Lessee. This

Indenture and the Lease Indenture Estate shall not be affected by any action taken under or in respect of the Trust Agreement except as otherwise provided in or permitted by this Indenture. The Trust Agreement may not in any event be terminated by the Equity Participant or the Owner Trustee or revoked by the Equity Participant so long as any of the Notes remain Outstanding or the lien of this Indenture has not been released. The Owner Trustee may resign as Owner Trustee, appoint a successor Owner Trustee and take all necessary and proper action to constitute one or more Persons as co-trustee(s) jointly with the Owner Trustee or as separate trustee(s), all in accordance with the terms and conditions of Article IX of the Trust Agreement.

SECTION 6.2. Indenture Events of Default.

The term Indenture Event of Default, wherever used herein, shall mean any of the following events (whatever the reason for such Indenture Event of Default, and whether it shall be voluntary or involuntary or come about or be effected by operation of law or pursuant to or in compliance with any judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

(a) any of the Events of Default specified in the following clauses of Section 15 of the Facility Lease: (1) clause (i)(y), except a failure of the Lessee to pay any amount which shall constitute an Excepted Payment; (2) clause (i)(x), except a failure of the Lessee to pay any amount which shall constitute an Excepted Payment or except where the Owner Trustee shall not have rescinded or terminated the Facility Lease pursuant to Section 16(a)(i) of the Facility Lease; or (3) clause (vii) or (x); or

(b) the rescission or termination of, or the taking of action by the Owner Trustee or the Equity Participant the effect of which would be to rescind or terminate, the Facility Lease, whether pursuant to Section 16(a)(i) of the Facility Lease or otherwise; or

(c) the exercise by the Owner Trustee or the Equity Participant of any of the remedies under Section 16(a)(v) of the Facility Lease prior to the happening of any of the events set forth in clause (b) of this Section 6.2; or

(d) any assignment, sublease or transfer by the Lessee in violation of Section 11(a) of the Facility Lease; or

(e) any failure by the Lessee to perform and observe Section 10(b)(3)(ii) or the first sentence of Section 10(b)(3)(i) of the Participation Agreement; or

(f) the Owner Trustee shall fail to make any payment in respect of the principal of, or premium, if any, or interest on, the Notes within five Business Days after the same shall have become due (other than by virtue of any failure by the Lessee to make any payment of Rent therefor); or

(g) the Owner Trustee shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 6.1 (other than clause (i) thereof), or the Equity Participant shall fail to perform or observe any covenant or agreement to be performed or observed by it under Section 7(b)(i) of the Participation Agreement, and, in any such case, such failure shall continue for a period of 30 days after notice thereof shall have been given to the Owner Trustee and the Equity Participant and the Lessee by the Indenture Trustee, specifying such failure and requiring it to be remedied; or

(h) any representation or warranty made by the Owner Trustee in Section 8(a) of the Participation Agreement, or any representation or warranty made by the Equity Participant in Section 7(a)(5) or (7) of the Participation Agreement, shall prove to have been incorrect in any material respect when such representation or warranty was made or given and remains material at the time of discovery thereof and, in any such case, the circumstances rendering such representation or warranty incorrect shall continue unremedied for a period of 30 days after notice thereof shall have been given to the Owner Trustee, the Equity Participant and the Lessee by the Indenture Trustee, specifying such circumstances and requiring them to be remedied, and the circumstances rendering such representation or warranty incorrect shall materially adversely affect the Holders of the Notes; or

(i) the Trust shall file any petition for dissolution or liquidation of the Trust or shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in

effect, or the Trust shall have consented to the entry of an order for relief in an involuntary case under any such law, or a receiver, custodian or trustee (or other similar official) shall be appointed for the Trust or shall take possession of any substantial part of its property (other than at the instance of the Indenture Trustee or the Noteholders), or the Trust shall make a general assignment for the benefit of its creditors, or shall enter into an agreement of composition with its creditors; or there shall be filed (other than at the instance of the Indenture Trustee or the Noteholders) against the Trust an involuntary petition in bankruptcy which results in an order for relief being entered or, notwithstanding that an order for relief has not been entered, the petition is not dismissed within 60 days of the date of the filing of the petition, or there shall be filed (other than at the instance of the Indenture Trustee or the Noteholders) under any Federal or state law relating to bankruptcy, insolvency or relief of debtors of any petition against the Trust for reorganization, composition, extension or arrangement with creditors which either (i) results in a finding or adjudication of insolvency of the Trust or (ii) is not dismissed within 60 days of the date of the filing of such petition; or

(j) the Equity Participant shall file any petition for dissolution or liquidation of the Equity Participant or shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or the Equity Participant shall have consented to the entry of an order for relief in an involuntary case under any such law, or shall fail generally to pay its debts as such debts become due (within the meaning of the Bankruptcy Code, or a receiver, custodian or trustee (or other similar official) shall be appointed for the Equity Participant or shall take possession of any substantial part of its property, or the Equity Participant shall make a general assignment for the benefit of its creditors, or shall enter into an agreement of composition with its creditors; or there shall be filed against the Equity Participant an involuntary petition in bankruptcy which results in an order for relief being entered or, notwithstanding that an order for relief has not been entered, the petition is not dismissed within 60 days of the date of the filing of the petition, or there shall be filed under any Federal or state law relating to bankruptcy, insolvency or relief of debtors of any petition against the Equity Participant for reorganization, composition,

extension or arrangement with creditors which either (i) results in a finding or adjudication of insolvency of the Equity Participant or (ii) is not dismissed within 60 days of the filing of such petition and any such event materially adversely affects the Holders of the Notes; or

(k) after a Special Transfer has been effected and amounts payable to the Equity Participant in connection therewith have been paid in full in accordance with Section 7(b)(4) of the Participation Agreement, any violation or breach of a warranty or covenant of the Lessee contained in the last paragraph of such Section 7(b)(4).

SECTION 6.3. Enforcement of Remedies.

(a) In the event that an Indenture Event of Default shall have occurred and be continuing, then and in every such case the Indenture Trustee, subject to paragraph (b) of this Section 6.3, may, and when required pursuant to the provisions of Article VII hereof shall, exercise any or all of the rights and powers and pursue, subject to any rights of the Lessee under the Facility Lease, (x) in the event such Indenture Event of Default (i) shall occur or be continuing after the effectiveness of a Special Transfer or assumption pursuant to Section 3.9(b) or (ii) is referred to in paragraph (f), (g), (h), (i), (j) or (k) of Section 6.2, any or all of the remedies then available pursuant to this Article VI and Article VII, or (y) subject to Section 6.11, in the event such Indenture Event of Default is referred to in paragraph (a), (b), (c), (d) or (e) of Section 6.2, any or all of such remedies concurrently with the exercise and pursuit by the Owner Trustee of any or all of the remedies then available to the Owner Trustee under the Facility Lease.

(b) Any provisions of the Facility Lease or this Indenture to the contrary notwithstanding, if the Lessee shall fail to pay any Excepted Payment to any Person entitled thereto as and when due, such Person shall have the right at all times, to the exclusion of the Indenture Trustee, to demand, collect, sue for, enforce performance of obligations relating to, or otherwise obtain all amounts due in respect of, such Excepted Payment.

SECTION 6.4. Specific Remedies; Enforcement of Claims without Possession of Notes.

Subject to Sections 6.2, 6.3 and 6.11 and the terms of the documents constituting a part of the Lease Indenture Estate, upon the occurrence and during the continuance of an Indenture Event of Default:

(a) The Indenture Trustee may, and upon receipt of a Directive shall, in order to enforce the rights of the Indenture Trustee and of the Holders of the Notes, direct payment to it of all moneys and enforce any agreement or undertaking constituting a part of the Lease Indenture Estate by any action, suit, remedy or proceeding authorized or permitted by this Indenture or by law or by equity, and whether for the specific performance of any agreement contained herein, or for an injunction against the violation of any of the terms hereof, or in aid of the exercise of any power granted hereby or by Applicable Law, and in addition may sell, assign, transfer and deliver, from time to time to the extent permitted by Applicable Law, all or any part of the Lease Indenture Estate or any interest therein, at any private sale or public auction with or without demand, advertisement or notice (except as herein required or as may be required by Applicable Law) of the date, time and place of sale and any adjournment thereof, for cash or credit or other property, for immediate or future delivery and for such price or prices and on such terms as the Indenture Trustee, in its uncontrolled discretion, may determine, or as may be required by Applicable Law, so long as the Equity Participant and the Owner Trustee are afforded a commercially reasonable opportunity to bid for all or such part of the Lease Indenture Estate in connection therewith. It is agreed that 90 days' notice to the Equity Participant, the Owner Trustee and the Lessee of the date, time and place of any proposed sale by the Indenture Trustee of all or any part of the Lease Indenture Estate or interest therein is reasonable. The Indenture Trustee may file such proofs of claim and other papers or documents as may be necessary or advisable in order to have the claims of the Indenture Trustee and of the Holders of the Notes asserted or upheld in any bankruptcy, receivership or other judicial proceedings. To the extent that any portion of the Lease Indenture Estate constitutes fixtures or real property, the Indenture Trustee shall have, to the extent not inconsistent with this Indenture, all the rights, remedies and benefits of a mortgagee of real property under Applicable Law

(including, without limitation, rights and remedies pursuant to Arizona Revised Statutes Section 33 - 702.B, or any comparable successor provision).

(b) Without limiting the foregoing, the Indenture Trustee, its assigns and its legal representatives, subject to the rights of the Lessee under the Facility Lease, shall have as to such of the Lease Indenture Estate as is subject to the Uniform Commercial Code or similar law in each relevant jurisdiction all the remedies of a secured party under the Uniform Commercial Code or similar law in such jurisdiction and such further remedies as from time to time may hereafter be provided in such jurisdiction for a secured party.

(c) All rights of action and rights to assert claims under this Indenture or under any of the Notes may be enforced by the Indenture Trustee without the possession of the Notes at any trial or other proceedings instituted by the Indenture Trustee, and any such trial or other proceedings shall be brought in its own name as trustee of an express trust, and any recovery or judgment shall be for the ratable benefit of the Holders of the Notes as herein provided. In any proceedings brought by the Indenture Trustee (and also any proceedings involving the interpretation of any provision of this Indenture to which the Indenture Trustee shall be a party) the Indenture Trustee shall be held to represent all the Holders of the Notes, and it shall not be necessary to make any such Holders parties to such proceedings.

(d) The Indenture Trustee may exercise any other right or remedy that may be available to it under Applicable Law or proceed by appropriate court action to enforce the terms hereof or to recover damages for the breach hereof.

(e) The Indenture Trustee agrees that the rights and remedies of the Indenture Trustee in the Undivided Interest, including the related Generation Entitlement Share, and, through the Real Property Interest, in the PVNGS Site are subject and subordinate to the rights and remedies of the ANPP Participants (other than (i) the Lessee or (ii) any Person who shall become an ANPP Participant in respect of the Lessor's Interest) under the ANPP Project Agreement.

(f) The Indenture Trustee agrees that, except as provided in Sections 15.2.2, 15.6.4 and 15.10 (or any

comparable successor provisions) of the ANPP Participation Agreement, the Lessee shall be and remain the sole "Participant" for all purposes of the ANPP Participation Agreement and the sole representative (with power to bind the Owner Trustee and the Indenture Trustee) in all dealings with the other ANPP Participants in relation to the property, rights, titles and interests of the Lessee transferred to the Owner Trustee pursuant to the Transaction Documents.

SECTION 6.5. Rights and Remedies Cumulative.

Subject to Sections 6.2, 6.3 and 6.11, (a) each and every right, power and remedy herein specifically given to the Indenture Trustee under this Indenture shall be cumulative and shall be in addition to every other right, power and remedy herein specifically given or now or hereafter existing at law, in equity or by statute, and each and every right, power and remedy whether specifically herein given or otherwise existing may be exercised from time to time and as often and in such order as may be deemed expedient by the Indenture Trustee, and the exercise or the beginning of the exercise of any right, power or remedy shall not be construed to be a waiver of the right to exercise at the same time or thereafter any other right, power or remedy, and (b) no delay or omission by the Indenture Trustee in the exercise of any right, power or remedy or in the pursuance of any remedy shall impair any such right, power or remedy or be construed to be a waiver of any default on the part of the Equity Participant, the Owner Trustee or the Lessee or to be an acquiescence therein.

SECTION 6.6. Restoration of Rights and Remedies.

In case the Indenture Trustee shall have proceeded to enforce any right, power or remedy under this Indenture by foreclosure, entry or otherwise, and such proceedings shall have been discontinued or abandoned for any reason or shall have been determined adversely to the Indenture Trustee, then and in every such case the Owner Trustee, the Equity Participant, the Indenture Trustee and the Lessee shall be restored to their former positions and rights hereunder with respect to the Lease Indenture Estate, and all rights, powers and remedies of the Indenture Trustee shall continue as if no such proceedings had been taken.

SECTION 6.7. Waiver of Past Defaults.

Any past Indenture Default or Indenture Event of Default and its consequences may be waived by the Indenture Trustee, except an Indenture Default or an Indenture Event of Default (i) in the payment of the principal of or premium, if any, or interest on any Note, subject to the provisions of Section 7.1, or (ii) in respect of a covenant or provision hereof which, under Section 10.2, cannot be modified or amended without the consent of each Holder of a Note then Outstanding. Upon any such waiver, such Indenture Default or Indenture Event of Default shall cease to exist, and any other Indenture Event 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 Indenture Default or Indenture Event of Default or impair any right consequent thereon.

SECTION 6.8. Right of Owner Trustee to Pay Rent; Note Purchase; Substitute Lessee.

Anything in this Article VI or Article VII to the contrary notwithstanding:

(a) an Indenture Event of Default shall be deemed cured if such Indenture Event of Default results from non-payment of Basic Rent or Supplemental Rent under the Facility Lease, and the Owner Trustee or the Equity Participant shall have paid all principal of and interest on the Notes due (other than by acceleration) on the date such Basic Rent was payable (plus interest on such amount as required hereby) within 15 days after the receipt by the Owner Trustee of notice of such non-payment, such receipt to be evidenced by, among other things, any notice thereof given to the Owner Trustee in accordance with the notice provisions of the Participation Agreement; provided, however, that (1) during the period that any Initial Series Notes are Outstanding, the Owner Trustee shall not be permitted to exercise its right to cure Indenture Events of Default under this clause (a) with respect to more than twelve consecutive dates on which Basic Rent is due and 24 such dates in the aggregate, and (2) during the period that the Refunding Notes are Outstanding, the Owner Trustee shall not be permitted to exercise its rights to cure Indenture Events of Default under this clause (a) with respect to more than two consecutive Basic Rent Payment Dates or on more than four Basic Rent Payment Dates

during the Lease Term. The Owner Trustee or the Equity Participant, upon exercising cure rights under this paragraph (a), shall not obtain any Lien on any part of the Lease Indenture Estate on account of such payment for the costs and expenses incurred in connection therewith nor, except as expressly provided in the succeeding sentence, shall any claims of the Owner Trustee or the Equity Participant against the Lessee or any other Person for the repayment thereof impair the prior right and security interest of the Indenture Trustee in and to the Lease Indenture Estate. Upon any payment by the Owner Trustee or the Equity Participant pursuant to this Section 6.8, the Owner Trustee or the Equity Participant, as the case may be, shall (to the extent of such payment made by it) be subrogated to the rights of the Indenture Trustee and the Holders of the Notes to receive the payment of Rent with respect to which the Owner Trustee or the Equity Participant made such payment and interest on account of such Rent payment being overdue in the manner set forth in the next sentence. If the Indenture Trustee shall thereafter receive such payment of Rent or such interest, the Indenture Trustee shall, notwithstanding the requirements of Section 5.1, on the date such payment is received by the Indenture Trustee, remit such payment of Rent (to the extent of the payment made by the Owner Trustee or the Equity Participant pursuant to this Section 6.8) and such interest to the Owner Trustee or the Equity Participant, as the case may be, in reimbursement for the funds so advanced by it, provided that if (i) any Indenture Event of Default hereunder shall have occurred and be continuing such payment shall not be remitted to the Owner Trustee or the Equity Participant but shall be held by the Indenture Trustee as security for the obligations secured hereby and distributed in accordance with Section 5.1 hereof, as appropriate, and provided, further that if the principal of and interest on the Notes shall have become due and payable pursuant to Section 7.1 hereof, such Rent and interest thereon shall be distributed by the Indenture Trustee in the order of priority set forth in Section 5.3 hereof.

(b) Each Holder of a Note agrees, by acceptance thereof, that if the Notes have been accelerated pursuant to Section 7.1, and the Owner Trustee, within 30 days after receiving notice from the Indenture Trustee pursuant to Section 7.1, shall give written notice to the Indenture Trustee of the Owner Trustee's intention to purchase all of the Notes in accordance with this paragraph, accompanied by assurances of the

Owner Trustee to purchase the Notes, then, upon receipt within 10 Business Days after such notice from the Owner Trustee of an amount equal to the aggregate unpaid principal amount of and any premium with respect to any unpaid Notes then held by such Holder, together with accrued but unpaid interest thereon to the date of such receipt (as well as any interest on overdue principal and, to the extent permitted by law, interest), such Holder will forthwith sell, assign, transfer and convey to the Owner Trustee (without recourse or warranty of any kind other than of title to the Notes so conveyed) all of the right, title and interest of such Holder in and to the Lease Indenture Estate, this Indenture and all Notes held by such Holder; provided, that no such Holder shall be required so to convey unless (1) the Owner Trustee shall have simultaneously tendered payment for all other Notes issued by the Owner Trustee at the time Outstanding pursuant to this paragraph and (2) such conveyance is not in violation of any Applicable Law.

(c) Each Holder of a Note further agrees by its acceptance thereof that the Owner Trustee shall have the right, pursuant to Section 16 of the Facility Lease, to terminate the Facility Lease and, in connection therewith, to arrange for the substitution of another Person as lessee under a new lease substantially similar to, and containing terms no less favorable to the Holders of the Notes than the terms of, the Facility Lease (hereinafter the Substituted Lessee) and, subject to: (i) any Indenture Event of Default under paragraphs (f), (g), (h), (i), (j) or (k) of Section 6.2 having been cured by the Owner Trustee, (ii) the Substituted Lessee's assuming all of the obligations under the Facility Lease and the Indenture Trustee having been provided with an opinion of counsel to the effect that the Substituted Lessee's assumption thereof is the valid and binding obligation of the Substituted Lessee and that no Governmental Actions (other than such as have been obtained) are required in connection with the Substituted Lessee's performance of the Facility Lease and (iii) the Substituted Lessee's having an assigned credit rating by Standard & Poor's Corporation and Moody's Investors Service, Inc. (or, if either of such organizations shall not rate securities issued by such Substituted Lessee, by any other nationally recognized rating organization in the United States of America) with respect to at least one series of its debt obligations or preferred stock equal to or better than the ratings assigned, immediately prior to such substitution, by such organizations to comparable

securities of the Lessee immediately prior to such substitution but in no event less than "investment grade" rating assigned by such organizations, the Facility Lease between the Owner Trustee and such Substituted Lessee shall, for all purposes of this Indenture, be deemed to be the Facility Lease subject to the lien of this Indenture.

SECTION 6.9. Further Assurances.

Subject to Section 7.6, the Owner Trustee covenants and agrees from time to time to do all such acts and execute all such instruments of further assurance as shall be reasonably requested by the Indenture Trustee for the purpose of fully carrying out and effectuating this Indenture and the intent hereof.

SECTION 6.10. Right of Indenture Trustee To Perform Covenants, etc.

If the Owner Trustee shall fail to make any payment or perform any act required to be made or performed by it hereunder or under the Facility Lease or if the Owner Trustee shall fail to release any Lien affecting the Lease Indenture Estate which it is required to release by the terms of this Indenture, the Indenture Trustee, without notice to or demand upon the Owner Trustee and without waiving or releasing any obligation or default, may (but shall be under no obligation to) at any time thereafter make such payment or perform such act for the account and at the expense of the Lease Indenture Estate. All sums so paid by the Indenture Trustee and all costs and expenses (including without limitation reasonable fees and expenses of legal counsel and other professionals) so incurred, together with interest thereon from the date of payment or occurrence, shall constitute additional indebtedness secured by this Indenture and shall be paid from the Lease Indenture Estate to the Indenture Trustee on demand. The Indenture Trustee shall not be liable for any damages resulting from any such payment or action unless such damages shall be a consequence of willful misconduct or gross negligence on the part of the Indenture Trustee.

SECTION 6.11. Certain Other Rights of the Owner Trustee.

(a) Except as otherwise provided in this Section 6.11, but notwithstanding any provision to the contrary in this Indenture, the Owner Trustee shall at

all times (other than during the period that the Indenture Trustee is entitled to exercise rights and powers and pursue remedies as provided in clause (x) of Section 6.3(a)) retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default, subject, however, to Section 10.2; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree to any amendment to, or any waiver, discharge or termination of, any term or provision of Sections 2(c), 3(g), 4, 7, 8(f)(iv), 9(i), 11, 15(i)(x), (i)(y), (vii) and (x) and the provisions affecting redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease.

(b) In the event that an Indenture Event of Default shall have occurred and be continuing, the Owner Trustee shall consult with the Indenture Trustee as to any proposed exercise or pursuit of remedies and the Indenture Trustee shall have the right, in its sole discretion, to cause the Owner Trustee to forbear from any such proposed action if the Indenture Trustee shall have determined that such action would have a material adverse effect on the Holders of the Notes ; provided, however, that the Owner Trustee shall not exercise or pursue remedies in a manner which would unreasonably deprive the Holders of the Notes of a material right or remedy unless the Owner Trustee is commensurately adversely affected.

Notwithstanding any provision of this Section 6.11 (other than Section 6.11(c)) to the contrary, the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the Stated Price) and (iii) the Owner Trustee shall not have notified the

Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date specified in the Owner Trustee's notice of election to purchase within 60 days after the date of such notice of election to purchase. If the Owner Trustee shall fail to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate at a price no lower than the Stated Price to any Person (other than the Indenture Trustee or a Holder or Holders of more than 25% of the Outstanding Bonds or Notes (including in each case Affiliates thereof)) at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the purchase price for the Lease Indenture Estate, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate.

(c) Notwithstanding any provision of this Indenture (including Section 6.11(b)) to the contrary, in no event shall the exercise of rights, powers and remedies by the Indenture Trustee cause the Owner Trustee to be in violation of Applicable Law nor shall the pursuit of such remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee (as defined in the ANPP Participation Agreement).

ARTICLE VII

CERTAIN DUTIES OF THE OWNER TRUSTEE AND THE INDENTURE TRUSTEE

SECTION 7.1. Duties in Respect of Events of Default, Deemed Loss Events and Events of Loss; Acceleration of Maturity.

In the event the Owner Trustee shall have actual knowledge of an Indenture Event of Default, an Event of Default, a Deemed Loss Event or an Event of Loss, the Owner Trustee shall give prompt written notice thereof to the Equity Participant, the Lessee and the Indenture Trustee. In the event the Indenture Trustee

shall have actual knowledge of an Event of Default, an Indenture Event of Default, a Deemed Loss Event or an Event of Loss, the Indenture Trustee shall give prompt written notice thereof to the Equity Participant, the Owner Trustee, the Lessee and each Holder of a Note. Subject to the terms of Sections 6.2, 6.3, 6.4, 6.8, 6.11 and 7.3, (a) the Indenture Trustee shall take such action (including the waiver of past Defaults in accordance with Section 6.7), or refrain from taking such action, with respect to any such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss as the Indenture Trustee shall be instructed by a Directive, (b) if the Indenture Trustee shall not have received instructions as above provided within 20 days after mailing by the Indenture Trustee of notice of such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss to the Persons referred to above, the Indenture Trustee may, subject to instructions thereafter received pursuant to the preceding sentence, take such action, or refrain from taking such action, but shall be under no duty to take or refrain from taking any action, with respect to such Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss as it shall determine advisable in the best interests of the Holders of the Notes of all series and (c) in the event that an Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee in its discretion may, or upon receipt of a Directive shall, by written notice to the Owner Trustee, declare the unpaid principal amount of all Notes with accrued interest thereon to be immediately due and payable, upon which declaration such principal amount and such accrued interest shall immediately become due and payable without further act or notice of any kind. For all purposes of this Indenture, in the absence of actual knowledge, neither the Owner Trustee nor the Indenture Trustee shall be deemed to have knowledge of an Indenture Event of Default or Event of Default except that the Indenture Trustee shall be deemed to have knowledge of the failure of the Lessee to pay any installment of Basic Rent within 5 Business Days after the same shall become due. For purposes of this Section 7.1, neither the Owner Trustee nor the Indenture Trustee shall be deemed to have actual knowledge of any Indenture Event of Default, Event of Default, Deemed Loss Event or Event of Loss unless it shall have received notice thereof pursuant to Section 11.6 or such Indenture Event of Default or Event of Default shall actually be known by an officer in the corporate trust department of the Owner Trustee or by an officer in the

Corporate Trustee Administration Department of the Indenture Trustee, as the case may be.

SECTION 7.2. Duties in Respect of Matters Specified in Directive.

Subject to the terms of Sections 6.2, 6.3, 6.4, 6.8, 6.11, 7.1 and 7.3, upon receipt of a Directive, the Indenture Trustee shall take such of the following actions as may be specified in such Directive: (i) give such notice or direction or exercise such right, remedy or power permitted hereunder or permitted with respect to the Facility Lease or in respect of any part or all of the Lease Indenture Estate as shall be specified in such Directive; and (ii) take such action to preserve or protect the Lease Indenture Estate as shall be specified in such Directive, it being agreed that without such a Directive, the Indenture Trustee shall not waive, consent to or approve any such matter as satisfactory to it.

SECTION 7.3. Indemnification.

The Indenture Trustee shall not be required to take or refrain from taking any action under Section 7.1 or 7.2 or Article VI which shall require the Indenture Trustee to expend or risk its own funds or otherwise incur any financial liability unless the Indenture Trustee shall have been indemnified by the Holders of the Notes against liability, cost or expense (including counsel fees) which may be incurred in connection therewith, or unless, in the reasonable judgment of the Indenture Trustee, the indemnities of the Lessee shall be adequate for such purpose; provided, however, that if the Holder of such Notes is the Collateral Trust Trustee, the unsecured written undertaking of the Collateral Trust Trustee, in its individual capacity, shall be sufficient indemnity for purposes of this Section. The Indenture Trustee shall not be required to take any action under Section 7.1 or 7.2 or Article VI nor shall any other provision of this Indenture be deemed to impose a duty on the Indenture Trustee to take any action, if the Indenture Trustee shall reasonably determine, or shall have been advised by counsel, that such action is likely to result in personal liability or is contrary to the terms hereof or of the Facility Lease or is otherwise contrary to law.

SECTION 7.4. Limitations on Duties; Discharge of Certain Liens Resulting from Claims Against Indenture Trustee.

The Indenture Trustee shall have no duty or obligation to take or refrain from taking any action under, or in connection with, this Indenture or the Facility Lease, except as expressly provided by the terms of this Indenture. The Indenture Trustee nevertheless agrees that it will, in its individual capacity and at its own cost and expense, promptly take such action as may be necessary duly to discharge all Liens on any part of the Lease Indenture Estate which result from acts by or claims against it arising out of events or conditions not related to its rights in the Lease Indenture Estate or the administration of the Lease Indenture Estate or the transactions contemplated hereby.

SECTION 7.5. Restrictions on Dealing with Lease Indenture Estate.

Except as provided in the Transaction Documents, the Owner Trustee shall not use, operate, store, lease, control, manage, sell, dispose of or otherwise deal with any part of the Lease Indenture Estate.

SECTION 7.6. Filing of Financing Statements and Continuation Statements.

Pursuant to Section 10(b)(2) of the Participation Agreement, the Lessee has covenanted to maintain the priority of the lien of this Indenture on the Lease Indenture Estate. The Indenture Trustee shall, at the request and expense of the Lessee as provided in the Participation Agreement, execute and deliver to the Lessee and the Lessee will file, if not already filed, such financing statements or other documents and such continuation statements or other documents with respect to financing statements or other documents previously filed relating to the lien created under this Indenture in the Lease Indenture Estate as may be necessary to protect, perfect and preserve the lien created under this Indenture. At any time and from time to time, upon the request of the Lessee or the Indenture Trustee, at the expense of the Lessee as provided in the Participation Agreement (and upon receipt of the form of document so to be executed), the Owner Trustee shall promptly and duly execute and deliver any

and all such further instruments and documents as the Lessee or the Indenture Trustee may request in order for the Indenture Trustee to obtain the full benefits of the lien, security interest and assignment created or intended to be created hereby and of the rights and powers herein granted. Upon the reasonable instructions (which instructions shall be accompanied by the form of document to be filed) at any time and from time to time of the Lessee or the Indenture Trustee, the Owner Trustee shall execute and file any financing statement (and any continuation statement with respect to any such financing statement), any certificate of title or any other document, in each case relating to the lien, security interest and assignment created by this Indenture, as may be specified in such instructions.. In addition, the Indenture Trustee and the Owner Trustee will execute such continuation statements with respect to financing statements and other documents relating to the lien created under this Indenture in the Lease Indenture Estate as may be reasonably specified from time to time in written instructions of any Holder of a Note (which instructions may, by their terms, be operative only at a future date and which shall be accompanied by the form of such continuation statement or other document so to be filed).

ARTICLE VIII

CONCERNING THE OWNER TRUSTEE AND THE INDENTURE TRUSTEE

SECTION 8.1. Acceptance of Trusts; Standard of Care.

The Indenture Trustee accepts the trusts hereby created and applicable to it and agrees to perform the same but only upon the terms of this Indenture and the Participation Agreement and agrees to receive and disburse all moneys constituting part of the Lease Indenture Estate in accordance with the provisions hereof, but no implied duties or obligations shall be read into this Indenture or the Participation Agreement against the Indenture Trustee. The Indenture Trustee shall enter into and perform its obligations under the Participation Agreement, and, at the request of the Owner Trustee, any other agreement relating to any transfer of the Undivided Interest or the Real Property

Interest or the assignment of rights under the Assignment and Assumption or, at the request of the Owner Trustee, the purchase by any Person of Notes or Additional Notes issued hereunder, all as contemplated hereby. The Indenture Trustee shall not be liable under any circumstances, except for its own willful misconduct or gross negligence. If any Indenture Event of Default shall have occurred and be continuing, the Indenture Trustee shall exercise such of the rights and remedies vested in it by this Indenture, subject to the provisions hereof, and shall use the same degree of care in their exercise as a prudent man would exercise or use in the circumstances in the conduct of his own affairs; but if in the opinion of the Indenture Trustee such action may tend to involve expense or liability, it shall not be obligated to take such action unless it is furnished with indemnity satisfactory to it.

SECTION 8.2. No Duties of Maintenance, Etc.

Except pursuant to Section 7.2 and except as provided in, and without limiting the generality of, Sections 7.1 and 7.4, the Indenture Trustee shall have no duty (i) to see to any recording or filing of any Transaction Document, or to see to the maintenance of any such recording or filing, or (ii) to see to the payment or discharge of any tax, assessment or other governmental charge or any lien or encumbrance of any kind owing with respect to, or assessed or levied against, any part of the Lease Indenture Estate (except such as are required to be paid or discharged by it pursuant to this Indenture or any of the other Transaction Documents) or to make or file any reports or returns related thereto.

SECTION 8.3. Representations and Warranties of Indenture Trustee and the Owner Trustee.

NONE OF THE OWNER TRUSTEE, THE INDENTURE TRUSTEE OR THE EQUITY PARTICIPANT MAKES ANY REPRESENTATION OR WARRANTY AS TO THE VALUE, CONDITION, MERCHANTABILITY OR FITNESS FOR USE OF UNIT 2, THE UNDIVIDED INTEREST OR ANY PART OF THE LEASE INDENTURE ESTATE OR AS TO ITS INTEREST THEREIN, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO UNIT 2, THE UNDIVIDED INTEREST OR ANY PART OF THE LEASE INDENTURE ESTATE WHATSOEVER. The Owner Trustee and the Indenture Trustee each represents and warrants, in its individual capacity, as to itself that this Indenture has been executed and delivered by one or more of its officers who are duly

authorized to execute and deliver this Indenture on its behalf.

**SECTION 8.4. Moneys Held in Trust;
Non-Segregation of Moneys.**

All moneys and securities deposited with and held by the Indenture Trustee under this Indenture for the purpose of paying, or securing the payment of, the principal of or premium or interest on the Notes shall be held in trust. Except as provided in Sections 2.4(c), 8.8 and 11.1, moneys received by the Indenture Trustee under this Indenture need not be segregated in any manner except to the extent required by law, and may be deposited under such general conditions as may be prescribed by law; provided, however, that any payments received or applied hereunder by the Indenture Trustee shall be accounted for by the Indenture Trustee so that any portion thereof paid or applied pursuant hereto shall be identifiable as to the source thereof. Except as otherwise expressly provided herein, the Indenture Trustee shall not be liable for any interest on any money held pursuant to this Indenture.

SECTION 8.5. Reliance on Writings, Use of Agents, Etc.

The Indenture Trustee shall incur no liability to anyone in acting upon any signature, instrument, notice, resolution, request, consent, telegram, order, certificate, report, opinion, bond or other document or paper believed by it to be genuine and believed by it to be signed by the proper party or parties. In the case of the Lessee, the Indenture Trustee may accept a copy of a resolution of the Board of Directors or any duly constituted and authorized committee of the Board of Directors of the Lessee, certified by the Secretary or an Assistant Secretary of the Lessee as duly adopted and in full force and effect, as conclusive evidence that such resolution has been duly adopted by such Board or Committee and that the same is in full force and effect. As to the aggregate unpaid principal amount of the Notes Outstanding as of any date, the Owner Trustee may for all purposes hereof rely on a certificate signed by any Authorized Officer of the Indenture Trustee. As to any fact or matter the manner of ascertainment of which is not specifically described herein, the Indenture Trustee may for all purposes hereof rely on a certificate, signed by the Chairman of the Board, the President, any Vice President and the Treasurer or the

Secretary or any Assistant Treasurer or Assistant Secretary of the Lessee, or a Holder of a Note or any Responsible Officer of the Owner Trustee, as the case may be, as to such fact or matter, and such certificate shall constitute full protection to the Indenture Trustee for any action taken or omitted to be taken by it in good faith in reliance thereon. The Indenture Trustee shall furnish to the Owner Trustee upon request such information and copies of such documents as the Indenture Trustee may have and as are necessary for the Owner Trustee to perform its duties under Article III. In the administration of the trusts hereunder, the Indenture Trustee may execute any of the trusts or powers hereof and perform its powers and duties hereunder directly or through agents or attorneys selected by it in good faith and with reasonable care, and, with respect to matters relating to the Notes, the Lease Indenture Estate and its rights and duties under this Indenture and the other Transaction Documents, may, at the expense of the Lessee, or, if the Lessee shall have failed to pay or provide for the payment thereof, at the expense of the Lease Indenture Estate, consult with counsel, accountants and other skilled persons to be selected and employed by it in good faith and with reasonable care, and the Indenture Trustee shall not be liable for anything done, suffered or omitted in good faith by it in accordance with the advice or opinion of any such counsel, accountants or other skilled persons so selected. Unless otherwise specified herein or in any other Transaction Document, any opinion of counsel referred to in this Indenture or in such other Transaction Document may be relied on by the Indenture Trustee to the extent it is rendered by an attorney or firm of attorneys satisfactory to the Indenture Trustee (which may be counsel to the Equity Participant, the Owner Trustee, the Lessee or any party to any Transaction Document).

SECTION 8.6. Indenture Trustee to Act Solely as Trustee.

The Indenture Trustee acts hereunder solely as trustee as herein provided and not in any individual capacity, except as otherwise expressly provided herein; and except as provided in Sections 9(a) and 9(b) of the Participation Agreement or Section 7.4 or 8.1, all Persons having any claim against the Indenture Trustee arising from matters relating to the Notes by reason of the transactions contemplated hereby shall, subject to the lien and priorities of payment as herein provided

and to Sections 3.6 and 5.7, look only to the Lease Indenture Estate for payment or satisfaction thereof.

SECTION 8.7. Limitation on Rights Against Registered Holders, the Owner Trustee or Lease Indenture Estate.

The Indenture Trustee shall be entitled to be paid or reimbursed for Trustee's Expenses as provided herein and in the other Transaction Documents. Nonetheless, the Indenture Trustee agrees that it shall have no right against the Holders of the Notes, the Owner Trustee (except to the extent included in Transaction Expenses payable by the Equity Participant) or, except as provided in Article V and Section 6.4 or this Article VIII, the Lease Indenture Estate for any fee as compensation for its services hereunder.

SECTION 8.8. Investment of Certain Payments Held by the Indenture Trustee.

Any amounts held by the Indenture Trustee hereunder other than pursuant to Section 2.3(c) or 11.1 shall be invested by the Indenture Trustee from time to time as directed in writing by the Owner Trustee or by the Equity Participant as agent of the Owner Trustee and at the expense and risk of the Equity Participant in (i) obligations of, or guaranteed as to interest and principal by, the United States Government maturing not more than 90 days after such investment, (ii) open market commercial paper of any corporation incorporated under the laws of the United States of America or any State thereof rated "prime-1" or its equivalent by Moody's Investors Service, Inc. or "A-1" or its equivalent by Standard & Poor's Corporation or (iii) certificates of deposit maturing within 90 days after such investment issued by commercial banks organized under the laws of the United States of America or of any political subdivision thereof having a combined capital and surplus in excess of \$500,000,000; provided, however, that the aggregate amount at any one time so invested (a) in open market commercial paper of any corporation shall not exceed \$2,000,000 and (b) in certificates of deposit issued by any one bank shall not exceed \$10,000,000. Any income or gain realized as a result of any such investment shall be applied to make up any losses resulting from any such investment to the extent such losses shall not have been paid by the Owner Trustee or the Equity Participant pursuant to this Section 8.8. Any further income or gain so realized

shall be promptly distributed (in no event later than the next Business Day) to the Owner Trustee or the Equity Participant, except after the occurrence and during the continuance of an Indenture Event of Default. The Indenture Trustee shall have no liability for any loss resulting from any investment made in accordance with this Section. Any such investment may be sold (without regard to maturity date) by the Indenture Trustee whenever necessary to make any distribution required by Article V.

SECTION 8.9. No Responsibility for Recitals, etc.

The Indenture Trustee makes no representation or warranty as to the correctness of any statement, recital or representation made by any Person other than the Indenture Trustee in this Indenture, any other Transaction Document or the Notes.

SECTION 8.10. Indenture Trustee May Engage in Certain Transactions.

The Indenture Trustee may engage in or be interested in any financial or other transaction with the Lessee, the Equity Participant, the Owner Trustee and any other party to a Transaction Document, provided that if the Indenture Trustee determines that any such relation is in conflict with its duties under this Indenture, it shall eliminate the conflict or resign as Indenture Trustee.

SECTION 8.11. Construction of Ambiguous Provisions.

The Indenture Trustee, subject to Section 8.1, may construe any ambiguous or inconsistent provisions of this Indenture, and any such construction by the Indenture Trustee shall be binding upon the Noteholders. In construing any such provision, the Indenture Trustee will be entitled to rely upon opinions of counsel and will not be responsible for any loss or damage resulting from reliance in good faith thereon, except for its own gross negligence or willful misconduct.

ARTICLE IX

SUCCESSOR TRUSTEES

SECTION 9.1. Appointment of Co-Trustees or Separate Trustees.

(a) At any time or times, when necessary or prudent or for the purpose of meeting the legal requirements of any jurisdiction in which any part of the Lease Indenture Estate may, at any time, be located, the Indenture Trustee, except as set forth in subsection (b)(6) of this Section 9.1, may, and upon receipt of a Directive shall, appoint one or more Persons to act as co-trustee of all or any such part of the Lease Indenture Estate or to act as separate trustee of any property constituting part thereof, in either case with such powers as may be provided in the instrument of appointment, and to vest in such Person or Persons any property, title, right or power deemed necessary or desirable, subject to the remaining provisions of this Section 9.1. Except as set forth in subsection (b)(6) of this Section 9.1 the Owner Trustee shall join in any such appointment upon the request of the Indenture Trustee, but such joining will not be necessary for the effectiveness of such appointment.

(b) Every separate trustee or co-trustee shall be appointed subject to the following terms:

(1) The rights, powers, duties and obligations conferred or imposed upon any such separate trustee or co-trustee shall not be greater than those conferred or imposed upon the Indenture Trustee, and such rights and powers shall be exercisable only jointly with the Indenture Trustee, except to the extent that, under any law of any jurisdiction in which any particular act or acts are to be performed, the Indenture Trustee shall be incompetent or unqualified to perform such act or acts, in which event, except as set forth in subsection (b)(6) of this Section 9.1, such rights and powers shall be exercised by such separate trustee or co-trustee subject to the provisions of subsection (b)(4) of this Section 9.1.

(2) The Indenture Trustee may at any time, by an instrument in writing executed by it, accept the resignation of, and may (and upon the receipt of a Directive, shall) remove any separate trustee or co-trustee appointed under this Section 9.1.

(3) No trustee, including the Indenture Trustee, under this Indenture shall be liable by reason of any act or omission of any other trustee or co-trustee under this Indenture.

(4) Except as set forth in subsection (b) (6) of this Section 9.1, no power given to such separate trustee or co-trustee shall be separately exercised hereunder by such separate trustee or co-trustee except with the consent in writing of the Indenture Trustee.

(5) The Indenture Trustee shall maintain custody of all money and securities.

(6) Notwithstanding anything contained to the contrary in this Section 9.1, to the extent the laws of any jurisdiction preclude the Indenture Trustee from taking any action hereunder either alone, jointly or through a separate trustee under the direction and control of the Indenture Trustee, the Owner Trustee, at the instruction of the Indenture Trustee, shall appoint a separate trustee for such jurisdiction, which separate trustee shall have full power and authority to take all action hereunder as to matters relating to such jurisdiction without the consent of the Indenture Trustee, but subject to the same limitations in any exercise of his power and authority as those to which the Indenture Trustee is subject.

(c) Upon the acceptance in writing of such appointment by any such separate trustee or co-trustee, it shall be vested with the estates or property to which its appointment relates as specified in the instrument of appointment, subject to all the terms of this Indenture.

(d) Any separate trustee or co-trustee may, at any time, constitute the Indenture Trustee, its agent or attorney-in-fact, with full power and authority, to the

extent not prohibited by law, to do any lawful act under or in respect of this Indenture on its behalf and in its name. If a separate trustee or co-trustee shall die, become incapable of acting, resign or be removed, all of its estates, properties, rights, remedies and trusts shall vest in and be exercised by the Indenture Trustee, to the extent permitted by law, without the appointment of a new or successor trustee.

SECTION 9.2. Resignation and Removal of Indenture Trustee; Appointment of Successor.

(a) The Indenture Trustee may resign at any time without cause by giving at least 30 days' prior written notice to the Equity Participant, the Owner Trustee, the Lessee and to each Holder of a Note, such resignation to be effective upon the acceptance of such trusteeship by a successor. In addition, the Indenture Trustee may be removed without cause by a Directive delivered to the Equity Participant, the Owner Trustee, the Lessee and the Indenture Trustee, and the Indenture Trustee shall promptly give notice thereof in writing to each Holder of a Note. In the case of the resignation or removal of the Indenture Trustee, a successor trustee may be appointed by such a Directive. If a successor trustee shall not have been appointed within 30 days after such notice of resignation or removal, the Indenture Trustee, the Owner Trustee or any Holder of a Note may apply to any court of competent jurisdiction to appoint a successor to act until such time, if any, as a successor shall have been appointed as above provided. The successor so appointed by such court shall immediately and without further act be superseded by any successor appointed as above provided within one year from the date of the appointment by such court.

(b) Any successor trustee, however appointed, shall execute and deliver to its predecessor and to the Owner Trustee an instrument accepting such appointment, and thereupon such successor, without further act, shall become vested with all the estates, properties, rights, powers and duties of its predecessor hereunder in the trusts under this Indenture applicable to it with like effect as if originally named the Indenture Trustee; but, nevertheless, upon the written request of such successor trustee or receipt of a Directive, its predecessor shall execute and deliver an instrument transferring to such successor trustee, upon the trusts herein expressly applicable to it, all the estates, properties, rights and powers of such predecessor under this

Indenture, and such predecessor shall duly assign, transfer, deliver and pay over to such successor trustee all moneys or other property then held by such predecessor under this Indenture.

(c) Any successor trustee, however appointed, shall be a bank or trust company organized under the laws of the United States or any jurisdiction thereof having a combined capital and surplus of at least \$100,000,000, if there be such an institution willing, able and legally qualified to perform the duties of the Indenture Trustee hereunder upon reasonable or customary terms.

(d) Any corporation into which the Indenture 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 Indenture Trustee shall be a party, or any corporation to which substantially all the corporate trust business of the Indenture Trustee may be transferred, shall, subject to the terms of paragraph (c) of this Section 9.1, be the Indenture Trustee under this Indenture without further act.

ARTICLE X

SUPPLEMENTS AND AMENDMENTS TO THIS INDENTURE AND OTHER DOCUMENTS

SECTION 10.1. Supplements, Amendments and Modifications to This Indenture Without Consent of Holders of Notes.

The Indenture Trustee may, with the written consent of the Owner Trustee, from time to time and at any time execute a supplement to this Indenture without the consent of the Holders of Notes Outstanding in order to (i) cure any defect, omission or ambiguity in this Indenture or for any other purpose if such action does not adversely affect the interests of such Holders, (ii) grant or confer upon the Indenture Trustee for the benefit of such Holders any additional rights, remedies, powers, authority or security which may be lawfully granted or conferred and which are not contrary to or inconsistent with this Indenture, (iii) add to the covenants or agreements to be observed by the Owner

Trustee and which are not contrary to or inconsistent with this Indenture or surrender any right or power of the Owner Trustee, (iv) confirm or amplify, as further assurance, any pledge under, and the attachment of, or subjection to any lien, security interest or pledge created or to be created by, this Indenture, of the properties covered hereby, or subject to attachment of, or the lien, security interest or pledge of this Indenture additional revenues, properties or other collateral, (v) qualify this Indenture under the provisions of the Trust Indenture Act, (vi) evidence the appointment of any successor Indenture Trustee pursuant to the terms hereof, (vii) evidence the assumption and release affected by the Assumption Agreement, or (viii) execute supplemental indentures to evidence the issuance of and to provide the terms of, Additional Notes to be issued hereunder in accordance with the terms hereof.

SECTION 10.2. Supplements and Amendments to this Indenture and the Facility Lease With Consent of Holders of Notes.

Except as provided in Section 10.1, at any time and from time to time, (i) upon receipt of a Directive, the Indenture Trustee shall execute a supplement to this Indenture for the purpose of adding provisions to, or changing or eliminating provisions of, this Indenture or for the purpose of consenting to the amendment to or waiver of Sections 2(c), 7, 8(f)(iv), 9(i), 11, 15(i)(x), 15(vii), 15(x) and 16 of the Facility Lease, but only as specified in such Directive, and (ii) upon receipt of a written instruction from the Lessee and the Owner Trustee, the Indenture Trustee shall consent to any amendment of or supplement to any Granting Clause Document otherwise than as provided in the proviso to Section 6.11(a) or execute and deliver such written waiver or modification of the terms of any Granting Clause Document otherwise than as provided in the proviso to Section 6.11(a); provided, however, that, without the consent of the Holders of all the Notes then Outstanding no such supplement or amendment to this Indenture or any Granting Clause Document, or waiver or modification of the terms of either thereof, shall (w) modify, waive, discharge or terminate any of the provisions of this Section or of Section 3.5, 7.1 or 7.2, or Sections 3(g), 4, 15(i)(y), and 14 (insofar as it affects redemption of the Notes) of the Facility Lease or of the definition of Directive contained in Appendix A hereto or the definition of Indenture Event of Default herein, reduce the amount of the Basic Rent

or Casualty Value or any payment under or pursuant to Section 16 of the Facility Lease as set forth in the Facility Lease below such amount as is required to pay the full principal of, and premium, if any, and interest on, the Notes when due, or extend the time of payment thereof, (x) otherwise modify, amend or supplement the Facility Lease in such manner as to reduce the Lessee's obligations in respect of the payment of the Basic Rent or Casualty Value or any payment under or pursuant to Section 16 of the Facility Lease below the amount referred to in clause (w) above, (y) except as provided in this Indenture, deprive the Holder of any Note of the lien of this Indenture on the Lease Indenture Estate or (z) materially adversely affect the rights and remedies for the benefit of such Holder provided in Article VI; and, provided, further, that, without the consent of the Holders of all the Notes then Outstanding and affected thereby, no such supplement or amendment to this Indenture or the Facility Lease, or waiver or modification of the terms of either thereof, shall reduce the amount or extend the time of payment of any amount payable under any Note, reduce or modify the provisions for the computation of the rate of interest owing or payable thereon, adversely alter or modify the provisions of Article V with respect to the order of priorities in which distributions thereunder with respect to the Notes shall be made, or reduce, modify or amend any indemnities in favor of the Holders of the Notes. Anything to the contrary contained herein notwithstanding, without the necessity of the consent of the Holders of Notes or the Indenture Trustee, (a) any indemnities in favor of the Owner Trustee or the Equity Participant may be modified, amended or changed and (b) the Owner Trustee may enter into any agreement with respect to the Lease Indenture Estate which by its terms does not become effective prior to the satisfaction and discharge of this Indenture, but any agreement entered into by the Owner Trustee pursuant to this clause (b) shall not materially adversely affect the Indenture Trustee or the Holder of any Note. Notwithstanding the foregoing, the Indenture Trustee shall, upon receipt of a written instruction from the Lessee and the Owner Trustee, consent to an amendment of any definitions contained in or appended to this Indenture which are being changed pursuant to the amendments, if any, referred to in Section 10(b)(3)(xii) of the Participation Agreement. The Owner Trustee shall deliver to the Indenture Trustee a copy of each amendment to the Facility Lease whether or not the Indenture Trustee is required to consent or otherwise act with respect thereto.

SECTION 10.3. Certain Limitations on Supplements and Amendments.

If in the opinion of the Owner Trustee or the Indenture Trustee, each of which shall be entitled to rely on counsel for purposes of this Section 10.3, any document required to be executed by either of them pursuant to the terms of Section 10.1 or 10.2 does not comply with the provisions of this Indenture or adversely affects any right, immunity or indemnity in favor of, or increases any duty of, the Owner Trustee or the Indenture Trustee under this Indenture, the Facility Lease or the Participation Agreement, the Owner Trustee or the Indenture Trustee, as the case may be, may in its discretion decline to execute such document.

SECTION 10.4. Directive Need Not Specify Particular Form of Supplement or Amendment.

It shall not be necessary for any Directive furnished pursuant to Section 10.2 to specify the particular form of the proposed documents to be executed pursuant to such Section, but it shall be sufficient if such request shall indicate the substance thereof.

SECTION 10.5. Trustee to Furnish Copies of Supplement or Amendment.

Promptly after the execution by the Owner Trustee or the Indenture Trustee of any document entered into pursuant to Section 10.2, the Indenture Trustee shall mail, by first-class mail, postage prepaid, a conformed copy thereof to each Holder of an Outstanding Note at the address of such Person set forth in the register kept pursuant to Section 4.1 but the failure of the Indenture Trustee to mail such conformed copies shall not impair or affect the validity of such document.

ARTICLE XI

MISCELLANEOUS

SECTION 11.1. Moneys for Payments in Respect of Notes to be Held in Trust.

In case the Holder of any Note shall fail to present the same for payment on any date on which the principal thereof or interest thereon becomes payable, the Indenture Trustee may set aside in trust the moneys then due thereon uninvested and shall pay such moneys to the Holder of such Note or such Person upon due presentation or surrender thereof in accordance with the provisions of this Indenture, subject always, however, to the provisions of Sections 3.8 and 11.2.

SECTION 11.2. Disposition of Moneys Held for Payments of Notes.

Any moneys set aside under Section 11.1 and not paid to Holders of Notes as provided in Section 11.1 shall be held by the Indenture Trustee in trust until the latest of (i) the date three years after the date of such setting aside, (ii) the date all other Holders of the Notes shall have received full payment of all principal of and interest and other sums payable to them on such Notes or the Indenture Trustee shall hold (and shall have notified such Persons that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due and (iii) the date the Owner Trustee shall have fully performed and observed all its covenants and obligations contained in this Indenture with respect to the Notes; and thereafter shall be paid to the Owner Trustee by the Indenture Trustee on demand; and thereupon the Indenture Trustee shall be released from all further liability with respect to such moneys; and thereafter the Holders of the Notes in respect of which such moneys were so paid to the Owner Trustee shall have no rights in respect thereof except to obtain payment of such moneys from the Owner Trustee. Upon the setting aside of such moneys, interest shall cease to accrue on the Notes.

SECTION 11.3. Transfers Not to Affect Indenture or Trusts.

No Holder of a Note shall have legal title to any part of the Lease Indenture Estate. No transfer, by operation of law or otherwise, of any Note or other right, title and interest of any Holder of a Note in and to the Lease Indenture Estate or hereunder shall operate to terminate this Indenture or the trusts hereunder with respect to such Note or entitle any successor or transferee of such Holder to an accounting or to the transfer to it of legal title to any part of the Lease Indenture Estate.

SECTION 11.4. Binding Effect of Sale of Lease Indenture Estate.

Any sale or other conveyance of the Lease Indenture Estate or any part thereof by the Indenture Trustee made pursuant to the terms of this Indenture or the Facility Lease shall bind the Holders of the Notes and shall be effective to transfer or convey all right, title and interest of the Indenture Trustee, the Owner Trustee and such Holders in and to the same. No purchaser or other grantee shall be required to inquire as to the authorization, necessity, expediency or regularity of such sale or conveyance or as to the application of any sale or other proceeds with respect thereto by the Indenture Trustee.

SECTION 11.5. Limitation as to Enforcement of Rights, Remedies and Claims.

Nothing in this Indenture, whether express or implied, shall be construed to give to any Person, other than the Owner Trustee, the Equity Participant, the Lessee (to the extent the Lessee's consent or other action by the Lessee is expressly provided for), the Indenture Trustee and the Holders of the Notes, any legal or equitable right, remedy or claim under or in respect of this Indenture or any Note.

SECTION 11.6. Notices.

Unless otherwise expressly specified or permitted by the terms hereof, all communications and notices given hereunder to the Lessee, the Owner Trustee, the Equity Participant or the Indenture Trustee shall be given in the manner provided in Section 18 of the Participation Agreement. Notices by the Indenture

Trustee to any Holder of a Note shall be in writing and shall be given in person or by means of telex, telecopy or other wire transmission (with request for assurance of receipt in a manner typical with respect to communications of that type), or mailed by registered or certified mail, addressed to such Holder at the address set forth in the register kept pursuant to Section 4.1. Whenever any notice in writing is required to be given by the Indenture Trustee to any Holder of a Note such notice shall be effective (x) if sent by telex, telecopy or other wire transmission, on the date of transmission thereof, or (y) if sent by mail, three Business Days after being mailed.

SECTION 11.7. Separability of Provisions

In case any one or more of the provisions of this Indenture or any application thereof shall be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions hereof and any other application hereof shall not in any way be affected or impaired.

SECTION 11.8. Benefit of Parties, Successors and Assigns.

All representations, warranties, covenants and agreements contained herein shall be binding upon, and inure to the benefit of, the Owner Trustee, the Indenture Trustee and their respective successors and assigns and each Holder of a Note, all as herein provided. Any request, notice, direction, consent, waiver or other instrument or action by any Holder of a Note shall bind the successors and assigns of such Holder and any Holder of a Note issued in transfer or exchange of such Note.

SECTION 11.9. Survival of Representations and Warranties.

All representations and warranties made with respect to the Notes shall survive the execution and delivery of this Indenture and the issue, sale and delivery of any Notes and shall continue in effect so long as any Note issued hereunder is Outstanding and unpaid.

SECTION 11.10: Bankruptcy of the Owner Trustee.

If (a) the Owner Trustee becomes a debtor subject to the reorganization provisions of the Bankruptcy Code, or any successor provision, (b) pursuant to such reorganization provisions the Owner Trustee is required, by reason of the Owner Trustee being held to have recourse liability directly or indirectly to the Holder of any Note or the Indenture Trustee, to make payment on account of any amount payable as principal or interest on such Note and (c) such Holder or the Indenture Trustee actually receives any Excess Amount (as hereinafter defined) which reflects any payment by the Owner Trustee on account of clause (b) of this Section, then such Holder or the Indenture Trustee, as the case may be, shall promptly refund to the Owner Trustee such Excess Amount. For purposes of this Section, "Excess Amount" means the amount by which such payment exceeds the amount which would have been received on or prior to the date of such payment by such Holder or the Indenture Trustee if the Owner Trustee had not become subject to the recourse liability referred to in clause (b) of this Section. Nothing contained in this Section shall prevent such Holder or the Indenture Trustee from enforcing any recourse obligation (and retaining the proceeds thereof) of the Owner Trustee expressly provided for under this Indenture.

SECTION 11.11. Bankruptcy of the Equity Participant.

The Indenture Trustee and the Holders of the Notes shall be bound by the provisions of Section 19(f) of the Participation Agreement.

SECTION 11.12. Counterpart Execution.

This Indenture and any amendment or supplement to this Indenture may be executed in any number of counterparts and by the different parties hereto and thereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument.

SECTION 11.13. Dating of Indenture.

Although this Indenture is dated for convenience and for the purpose of reference as of the date mentioned, the actual date or dates of execution by the Owner Trustee and the Indenture Trustee are as indicated by their respective acknowledgments hereto annexed.

SECTION 11.14. Applicability of Annex A.

Notwithstanding any provision of this Indenture to the contrary, at all times that any Initial Series Notes are Outstanding, the terms and provisions of Annex A hereto shall supercede any contrary or inconsistent provision of this Indenture.

IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Indenture to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Emerson Finance Co.

By 
Assistant Vice President

CHEMICAL BANK,

By _____
Vice President

IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Indenture to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Emerson Finance Co.

By _____
Assistant Vice President

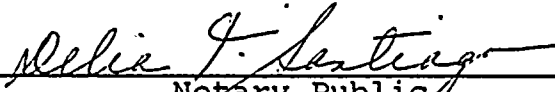
CHEMICAL BANK,

By _____
Vice President



STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 17th day of August, 1986, before me personally came Martin P. Henry, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Scituate, Massachusetts; that he is an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, described in and which executed the foregoing instrument; that he knows the seal of said association; that the seal affixed to said instrument is such seal; that it was so affixed by authority of the by-laws of said association; and that he signed his name thereto on behalf of said association by like order.


Notary Public

[NOTARIAL SEAL]

Term Expires:

DELIA T. SANTIAGO
Notary Public, State of New York
No. 41-3451102
Qualified in Queens County
Commission Expires March 22, 1987

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 17th day of August, 1986, before me personally came JOHN J. FLEMING, to me known, who, being by me duly sworn, did acknowledged, depose and say that he resides at Brooklyn, New York; that he is Vice President of CHEMICAL BANK, a New York banking corporation, described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such seal; that it was so affixed by authority of the board of directors of said corporation; and that he signed his name thereto on behalf of said corporation by like order.

Anna Marie Napoli
Notary Public

[NOTARIAL SEAL]

Term Expires:

ANNA MARIE NAPOLI
Notary Public, State of New York
No. 24-4759283
Qualified in Kings County
Certificate Filed in New York County
Commission Expires August 31, 19...88

EXHIBIT A

FORM OF INITIAL SERIES NOTE

The Initial Series Note shall be substantially in the following form, with such omissions, insertions and variations as the Owner Trustee may determine with the approval of the Indenture Trustee and are not inconsistent with the provisions of the Indenture or as may be provided for in the Indenture:

THIS NOTE HAS NOT BEEN REGISTERED
UNDER THE SECURITIES ACT OF 1933 AND
MAY NOT BE TRANSFERRED, SOLD OR OFFERED
FOR SALE IN VIOLATION OF SUCH ACT.

NONRECOURSE PROMISSORY NOTE, INITIAL SERIES.

No. _____ August __, 19 __
\$ _____

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity but solely as Owner Trustee ("Owner Trustee") under a Trust Agreement dated as of August 1, 1986 with _____ as Equity Participant, hereby promises to pay to _____ ("Lender"), or registered assigns, the principal sum of _____ DOLLARS (\$ _____) (the "Loan"), such payment to be made in semiannual installments on June 30 and December 30 of each year beginning December 30, 1986, and ending December 30, 2015, each installment to be in an amount equal to the original principal amount of this Initial Series Note ("Note") multiplied by the percentage set forth opposite the applicable date on Schedule 1 attached hereto, provided that the remaining unpaid principal amount of this Note, together with all accrued but unpaid interest, shall in any and all cases, be due and payable on December 30, 2015; and to pay interest on such principal amount from time to time outstanding hereunder at the rates, and in the manner and at the times specified below. Principal, interest and all other sums payable hereunder are payable in lawful money of the United States of America ("Dollars") no later than 10:00 a.m. (Los Angeles time) on the day when due in funds immediately available to Bank of America National Trust and Savings Association ("Bank of America") acting in its capacity as agent for Lender ("Agent") at Bank of America Corporate Service Center North, Department 1233, 1850 Gateway Boulevard, Concord, California 94520, Attention: Ms. Julie Hopkins (re: Arizona Public Service Company), or at such other place as Agent shall designate, for the account of Lender. As between Owner Trustee and Lender, payments to Agent constitute payments to Lender.

This Note is one of the Notes referred to in, and is entitled to the collateral and other benefits of, the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986 as amended or

supplemented in accordance with the provisions thereof (the "Indenture"), among Owner Trustee and Chemical Bank as Indenture Trustee, which Indenture provides for the acceleration of the maturity hereof upon the happening of certain stated events and for the obligation and the right of Owner Trustee to prepay the principal prior to the maturity hereof, in each case upon the terms and conditions therein and herein specified. Capitalized terms used in this Note which are not otherwise defined herein shall have the meanings ascribed to them in the Indenture.

1. Interest

Interest on the Loan shall be payable at the Variable Rate, provided, however, that during the period commencing on the date of this Note and ending on December 30, 1986 ("Option Period"), Owner Trustee may select in accordance with Paragraph 10 below, an interest rate applicable to the Loan equal to the Adjusted Eurodollar Rate. Notwithstanding the foregoing or any other provision of this Note, (i) the entire outstanding principal balance of this Note shall at all times be either a single Variable Rate Loan (as defined below) or a single Eurodollar Loan (as defined below), and (ii) Adjusted Eurodollar Rate shall not be applicable after December 30, 1986.

(a) "Variable Rate" shall mean the Applicable Percentage (as defined below) of the rate publicly announced from time to time by Bank of America in San Francisco, California, as its Reference Rate. Such rate is set by Bank of America based upon various factors, including Bank of America's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans; loans may be priced at, above or below the Reference Rate. Any change in the Variable Rate shall take effect on the day specified in the public announcement of such change; provided that in no event shall any such change take effect prior to the date of such announcement. While bearing interest at the Variable Rate, the Loan shall be referred to herein as the "Variable Rate Loan." "Applicable Percentage" shall equal (i) 100% for the period commencing on the date of this Note and ending December 31, 1986, (ii) 125% for the period commencing January 1, 1987, and ending May 31, 1987, (iii) 150% for the period commencing June 1, 1987, and ending August 31, 1987, and (iv) 200% thereafter.

(b) "Adjusted Eurodollar Rate" shall mean with respect to any Interest Period (as defined below), the percentage rate of interest per annum equal to 1.50 percent above the Eurodollar Rate. While bearing interest at the Adjusted Eurodollar Rate, the Loan shall be referred to

herein as a "Eurodollar Loan." "Eurodollar Rate" shall mean the per annum rate of interest determined by Agent to be the arithmetic mean, expressed as a percentage (rounded upwards, if necessary, to the nearest 1/100 of 1%), of the rates of interest per annum quoted to the Agent by each of Bank of America, Mellon Bank, and Chemical Bank (each a "Reference Bank" and collectively "Reference Banks") as the rate of interest per annum, net of reserves referred to in subparagraph (c) of Paragraph 3 below, at which Dollar deposits for such Interest Period and in the approximate aggregate amount of the Eurodollar Loans being maintained by such Reference Bank on the first day of such Interest Period under this Note and the Other Notes (as defined below) would be offered by such Reference Bank to major banks in the London inter-bank market upon request of such banks at approximately 11:00 a.m. (London time) three (3) Business Days before the commencement of such Interest Period. If any one of the Reference Banks shall be unable or shall otherwise fail to notify a rate, the mean rate shall be determined on the basis of the rate or rates notified by the other Reference Banks. "Other Notes" shall mean all other Initial Series Notes issued pursuant to the Indenture.

(c) "Interest Period" shall mean the period commencing on the date designated as the effective date of such Interest Period by Owner Trustee by notice to Agent in accordance with Paragraph 10 and ending on the numerically corresponding day of the next succeeding calendar month or, if there is no such numerically corresponding day, on the last day of such next succeeding calendar month; provided, however, that:

(i) if any Interest Period would end on a day that is not a Business Day, such Interest Period shall be extended to the next succeeding Business Day unless, such next succeeding Business Day would fall in the next calendar month, in which case such Interest Period shall end on the next preceding Business Day; and

(ii) the duration of any Interest Period which would otherwise end after the last day of the Option Period shall end on such last day.

2. Payment of Interest

Interest on the Loan shall accrue from the date made until paid in full at the applicable rate in effect from time to time and shall be payable as follows (a) as to the Variable Rate Loan, interest shall be payable monthly, in arrears, on the 30th day of such month, and (b) as to the Eurodollar Loan, interest shall be payable on the last day of each Interest Period with respect thereto; provided,

however, that interest shall accrue and be payable to the extent permitted by applicable law, on any amount that shall be overdue at a rate per annum equal to 2% over the interest rate then otherwise applicable under this Note, payable on demand by Agent.

3. Prepayment

(a) Premium. Upon at least five (5) Business Days' notice to Agent and provided that all the Other Notes shall concurrently be prepaid in whole in accordance with their respective terms, the outstanding principal amount of this Note may be prepaid but only in whole and not in part, and together with all accrued interest to the date of such prepayment, and together with any amount payable under subparagraph (c) of paragraph 8 below, and any premium in an amount calculated as a percentage of the original stated principal amount as follows: (i) .096% for the period from the date of this note through August 26, 1986, (ii) .072% for the period August 27, 1986 through September 2, 1986, (iii) .043% for the period September 3, 1986 through September 9, 1986, (iv) .024% for the period September 10, 1986 through September 16, 1986, and (v) none thereafter.

(b) Mandatory Prepayment. The unpaid principal balance outstanding under this Note shall be due and payable in full, together with interest accrued to the date of such payment, and premium, if any, calculated in accordance with subparagraph (a) above, and all other amounts due hereunder upon the occurrence of any of the following:

(i) Section 3.5 of the Indenture to the contrary notwithstanding, on the date of the issuance of any Additional Notes; or

(ii) upon the occurrence of any Indenture Event of Default, but only as provided in the Indenture.

4. Application of Payments

The Holder, by its acceptance of this Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. Holder further agrees, by its acceptance hereof, to duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Note unless and until all such notations have been duly made; provided, that neither the failure to make any such notation nor the inaccuracy of any such notation shall operate, or be deemed, to modify or impair any obligation of Owner Trustee hereunder.

5. Computations

All computations hereunder of interest on the Loan at the Adjusted Eurodollar Rate shall be based on a 360-day year and actual days elapsed, including the first day but excluding the last day; interest at the Variable Rate shall be computed on the basis of a year of 365 or 366 days, as the case may be.

6. Lending Offices

The Loan shall be made and maintained at any office designated by Lender from time to time for such purposes ("Lending Office"); provided, however, that the location of any such Lending Office shall not affect the obligation of Owner Trustee to repay the Loan at the Agent's office as provided above.

7. Payment on Non-Business Day

Subject to clause (i) of subparagraph (c) of Paragraph 1 above, whenever any payment to be made hereunder is stated to be due on a day that is not a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall be included in the computation of payment of interest.

8. Change in Circumstances Affecting Eurodollar Loans, Reserve Requirements, etc.

(a) Inability to Determine Eurodollar Rate. If at any time during the Option Period, Agent shall determine (which determination shall be made in good faith and shall be conclusive and binding upon Owner Trustee) that (i) by reason of circumstances then affecting the London interbank market, adequate and reasonable means do not or will not exist for ascertaining the interest rate applicable to a Eurodollar Loan, or (ii) Dollar deposits in the relevant amounts and for the relevant Interest Period are not available to the Lender in the London inter-bank market, then Agent shall forthwith give notice of such determination to the Owner Trustee at least one Business Day prior to the first day of any Interest Period so affected, whereupon, until Agent shall notify Owner Trustee that the circumstances giving rise to such suspension no longer exist (which notice shall be promptly given by Agent on discovery of such non-existence), (i) if the Variable Rate Loan is then outstanding, the obligations of the Lender to convert the Loan to a Eurodollar Loan shall be suspended and (ii) if the Eurodollar Loan is then outstanding, such Eurodollar Loan shall, automatically, on the last day of the then

current Interest Period therefor convert into a Variable Rate Loan.

(b) Illegality. If, after the date hereof, the introduction of or any change in any applicable law, rule or regulation or in the interpretation or administration thereof by any governmental authority charged with the interpretation or administration thereof or compliance by Lender with any request or directive (whether or not having the force of law) of any such authority shall make it unlawful or impractical for Lender (or its Lending Office) to make, maintain or fund its Eurodollar Loan, Lender shall forthwith give notice thereof to Agent and Owner Trustee. Before giving any notice pursuant to this subparagraph (b), Lender shall designate a different Lending Office if such designation will avoid the need for giving such notice and will not be otherwise disadvantageous to Lender in the sole judgment of Lender. Upon receipt of such notice (i) any pending conversion of the Loan into a Eurodollar Loan shall be withdrawn and the Loan shall continue instead as a Variable Rate Loan; and (ii) any outstanding Eurodollar Loan shall be automatically converted to a Variable Rate Loan, without premium or penalty, upon (x) the last day of the then current Interest Period if Lender may lawfully continue to fund and maintain such Eurodollar Loan to such day or (y) immediately if Lender may not lawfully continue to fund and maintain such affected Eurodollar Loan to such day.

(c) Reserve Requirements. Without limiting the effect of subparagraph (d) of this Paragraph 8, upon notice by Lender to Owner Trustee, Owner Trustee shall pay to Lender on the last day of each Interest Period for a Eurodollar Loan so long as Lender may be required to maintain reserves against "Eurocurrency liabilities" under (and as defined in) Regulation D of the Board of Governors of the Federal Reserve System (the "Board"), as additional interest on the unpaid principal amount of such Eurodollar Loan, an additional amount equal to such amount as would, together with payments of interest on such Eurodollar Loan for such Interest Period, result in the receipt by Lender of total interest on such Eurodollar Loan for such Interest Period at a rate equal to the rate determined in accordance with the following formula:

Adjusted Eurodollar Rate, divided by one
(1) minus the rate (expressed as a
decimal) of such reserves then required
by such Regulation D.

In determining the additional amount payable pursuant to this subparagraph (c) for any Interest Period, Lender shall (i) calculate the effect of reserve requirements in respect of Eurocurrency liabilities on its Eurodollar Loan as though

it had funded such Loan in the offshore Dollar market (whether or not so funded), without an offset or credit for such advances as Lender may make or may have made to its offshore branches or affiliates and (ii) take into account any transitional adjustment or phase-in provisions of such reserve requirements, applicable during such Interest Period, which would reduce the reserve requirement otherwise applicable to Eurocurrency liabilities during such Interest Period. Each such determination made by Lender, and each such notification by Lender to Owner Trustee under this subparagraph (c), shall be conclusive as to the matters therein as set forth in the absence of manifest error.

(d) Increased Cost. If any present or future applicable law, rule or regulation or any change therein or in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof or compliance by Lender (or its Lending Office) with any request or directive of any such authority, central bank or comparable agency, whether or not having the force of law:

(i) shall subject Lender (or its Lending Office) to any tax, duty or other charge with respect to the Eurodollar Loan or its obligation to make a Eurodollar Loan, or shall change the basis of taxation of payments to such Lender (or its Lending Office) of the principal of or interest with respect to its Eurodollar Loan, or in respect of any other amounts due under this Note in respect of its Eurodollar Loan, or its obligation to make a Eurodollar Loan (except for changes in the rate of tax on the overall net income of Lender or its Lending Office imposed by the jurisdiction in which such Lender's principal executive office or Lending Office is located); or

(ii) shall impose, modify or deem applicable any reserve (including, without limitation, any imposed by the Board), special deposit, compulsory loan or similar requirement against assets of, or deposits or other liabilities with, of or for the account of, or credit extended by, or shall impose on Lender (or its Lending Office), the London inter-bank market any other condition, affecting Lender's Eurodollar Loan, or its obligation to convert to a Eurodollar Loan;

and the result of any of the foregoing would in the opinion of Lender increase the cost to Lender (or its Lending Office) of making or maintaining its Eurodollar Loan, or reduce the amount of any sum received or receivable by

Lender (or its Lending Office) under this Note by an amount deemed by Lender to be material, then, within fifteen (15) days after written demand by Lender delivered to Owner Trustee by Agent, Owner Trustee will pay such additional amount or amounts as would compensate such Lender for increased cost or reduction. Lender will designate a different Lending Office if such designation will avoid the need for, or reduce the amount of, such compensation and will not be otherwise disadvantageous to Lender in the sole discretion of Lender. A certificate of Lender setting forth such additional amount or amounts necessary to compensate the Lender shall be conclusive in the absence of manifest error.

(e) Funding Indemnification. If, during the Option Period, Owner Trustee makes any payment of principal with respect to the Eurodollar Loan on a day other than the last day of the then current Interest Period, Owner Trustee shall reimburse Lender on demand for any loss incurred by it as a result of the timing of such payment not reflected in the Eurodollar Rate, including without limitation any loss incurred in liquidating or employing deposits from third parties and loss of profit for the period after such payment. A certificate of Lender setting forth the amounts necessary so as to reimburse it in respect of any loss shall be conclusive and binding absent manifest error.

(f) Funding of Eurodollar Loans. Lender is entitled to fund its Eurodollar Loan in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though Lender had actually funded the Eurodollar Loan through the purchase of offshore Dollar deposits in the London inter-bank market in the relevant amount and in maturities corresponding to the relevant Interest Period.

9. Taxes, Set-Off and Counterclaims with Respect to Eurodollar Loan

Owner Trustee will pay to Agent for the account of Lender all amounts of principal, interest, premium and other fees and all other amounts due hereunder without set-off or counterclaim and free and clear of, and without deduction or withholding for or on account of, any present or future taxes, levies, imports, duties, assessments, restrictions, conditions or other charges of whatever nature, and all interest, penalties or similar liabilities with respect thereto, now or hereafter imposed, levied, collected, withheld or assessed by any country or by any political subdivision or taxing authority thereof or therein, on or with regard to the Eurodollar Loan contemplated in or by this Note, excluding income and franchise taxes of the

United States of America, or any political subdivision or taxing authority thereof or therein, and of the country in which Lender's Lending Office is located or any political subdivision or taxing authority thereof or therein.

In the event Owner Trustee is prohibited by operation of law from (i) making payments without deduction as provided hereinabove, or (ii) paying, causing to be paid, or reimbursing Lender for the cost of, any and all taxes, fees or other charges as provided hereinabove, then payments due to Lender under this Note shall be increased to such amount which, after provision for such taxes, fees or other charges, is necessary to yield and remit to Lender payments at the applicable rate specified in this Note.

Owner Trustee will furnish to Lender and Agent certified copies of tax receipts evidencing the payment of the amounts so levied or imposed within 90 days after the date any such payment is due pursuant to applicable law, unless any Lender shall have paid such tax or levy directly and received a receipt therefor.

10. Notices of Interest Rate Selection;
Failure to Provide Notice

Article III of the Indenture to the contrary notwithstanding, notices by Owner Trustee to Agent of prepayment of the Loan and of the conversion of the Loan from a Variable Rate Loan to a Eurodollar Loan or of the continuation of the Eurodollar Loan through the next succeeding Interest Period (together, in the case of each such conversion or continuation, with notice of the applicable Interest Period) shall be in writing (or by telephone promptly confirmed in writing) and shall be irrevocable and shall be effective only if received by Agent not later than 10:00 a.m. (Los Angeles time) ten (10) Business Days (in case of prepayment) and four (4) Business Days (in case of conversion or continuation) prior to the date of the relevant prepayment or the commencement of the applicable Interest Period, as the case may be; provided, however, that if Agent does not timely receive such notice of conversion to, or continuation of, the Eurodollar Loan, the Loan shall continue as, or convert (as of the last day of the current Interest Period) to, a Variable Rate Loan. Each such notice of prepayment, continuation or conversion shall specify (i) for any such prepayment or conversion, the date thereof, and (ii) for any such continuation or conversion, the duration of the applicable Interest Period.

11. Certain Miscellaneous Provisions

All payments, including payments of principal, premiums, if any, interest, and other sums to be made by Owner Trustee hereunder or under the Indenture shall be made only from the Lease Indenture Estate; and the Holder hereof, by its acceptance of this Note, agrees that such Holder will look solely to the Lease Indenture Estate and that Owner Trustee except as otherwise expressly provided in the Indenture is not personally liable to the Holder hereof for any amounts payable under this Note or the Indenture or any other Transaction Document; provided, however, that nothing in this paragraph shall be deemed or construed to limit or impair any right of the Indenture Trustee to declare an Indenture Event of Default, to accelerate the maturity of this Note, to declare the unpaid principal balance hereof to be due and payable in full, or otherwise to exercise any and all rights and remedies available under the Indenture, all as and to the extent provided in the Indenture.

This Note shall be construed and enforced in accordance with and governed by the law of New York applicable to contracts made and to be performed entirely within such State.

IN WITNESS WHEREOF, the Owner Trustee has caused this Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with _____.

By: _____

Title: _____

This Note is one of the
series of Notes referred to
therein and in the within-
mentioned Indenture.

CHEMICAL BANK
as Indenture Trustee,

By: _____
Authorized Officer

Schedule 1

Amortization of Initial Series Note

Amounts Stated as a percent of Original Principal

Original Principal Amount as a percent of Facility Cost : 78.3117544%

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
12/30/1986	2.9333333	2.9333333	0.0000000	100.0000000	8.00%
6/30/1987	5.3854120	5.0750000	0.3104120	99.6895880	10.15%
12/30/1987	5.3854120	5.0592466	0.3261654	99.3634226	10.15%
6/30/1988	5.3854120	5.0426937	0.3427183	99.0207044	10.15%
12/30/1988	5.3854120	5.0253007	0.3601112	98.6605931	10.15%
6/30/1989	5.3854120	5.0070251	0.3783869	98.2822063	10.15%
12/30/1989	5.3854120	4.9878220	0.3975900	97.8846163	10.15%
6/30/1990	5.3854120	4.9676443	0.4177677	97.4668486	10.15%
12/30/1990	5.3854120	4.9464426	0.4389694	97.0278792	10.15%
6/30/1991	5.3854120	4.9241649	0.4612471	96.5666320	10.15%
12/30/1991	5.3854120	4.9007566	0.4846554	96.0819766	10.15%
6/30/1992	5.3854120	4.8761603	0.5092517	95.5727250	10.15%
12/30/1992	5.3854120	4.8503158	0.5350962	95.0376288	10.15%
6/30/1993	5.3854120	4.8231597	0.5622523	94.4753765	10.15%
12/30/1993	5.3854120	4.7946254	0.5907866	93.8845899	10.15%
6/30/1994	5.3854120	4.7646429	0.6207690	93.2638208	10.15%
12/30/1994	5.3854120	4.7331389	0.6522731	92.6115478	10.15%
6/30/1995	5.3854120	4.7000360	0.6853759	91.9261718	10.15%
12/30/1995	5.3854120	4.6652532	0.7201588	91.2060131	10.15%
6/30/1996	5.3854120	4.6287052	0.7567068	90.4493063	10.15%
12/30/1996	5.3854120	4.5903023	0.7951097	89.6541966	10.15%
6/30/1997	5.3854120	4.5499505	0.8354615	88.8187351	10.15%
12/30/1997	6.5821701	4.5075508	2.0746193	86.7441158	10.15%
6/30/1998	6.5821701	4.4022639	2.1799062	84.5642095	10.15%
12/30/1998	6.5821701	4.2916336	2.2905365	82.2736731	10.15%
6/30/1999	6.5821701	4.1753889	2.4067812	79.8668919	10.15%
12/30/1999	6.5821701	4.0532448	2.5289254	77.3379665	10.15%
6/30/2000	6.5821701	3.9249018	2.6572683	74.6806982	10.15%
12/30/2000	6.5821701	3.7900454	2.7921247	71.8885735	10.15%
6/30/2001	5.9814313	3.6483451	2.3330862	69.5554873	10.15%
12/30/2001	5.0408577	3.5299410	1.5109167	68.0445706	10.15%
6/30/2002	5.2799583	3.4532620	1.8266964	66.2178742	10.15%
12/30/2002	4.9521294	3.3605571	1.5915723	64.6263019	10.15%
6/30/2003	5.2067660	3.2797848	1.9269812	62.6993207	10.15%
12/30/2003	4.8605733	3.1819905	1.6785827	61.0207380	10.15%
6/30/2004	5.1295660	3.0968025	2.0327636	58.9879744	10.15%
12/30/2004	4.7640002	2.9936397	1.7703605	57.2176139	10.15%
6/30/2005	5.0481360	2.9037939	2.1443421	55.0732718	10.15%
12/30/2005	4.6621356	2.7949685	1.8671670	53.2061048	10.15%
6/30/2006	4.9622442	2.7002098	2.2620344	50.9440704	10.15%
12/30/2006	4.5546895	2.5854116	1.9692779	48.9747925	10.15%
6/30/2007	4.8716461	2.4854707	2.3861754	46.5886172	10.15%
12/30/2007	4.4413560	2.3643723	2.0769837	44.5116335	10.15%
6/30/2008	4.7760838	2.2589654	2.5171184	41.9945151	10.15%
12/30/2008	4.3218127	2.1312216	2.1905911	39.8039239	10.15%

Schedule 1 - con't.

Amortization of Initial Series Note

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
6/30/2009	4.6752854	2.0200491	2.6552362	37.1486877	10.15%
12/30/2009	4.1957193	1.8852959	2.3104234	34.8382643	10.15%
6/30/2010	4.5689639	1.7680419	2.8009220	32.0373423	10.15%
12/30/2010	4.0627168	1.6258951	2.4368217	29.6005207	10.15%
6/30/2011	4.4568167	1.5022264	2.9545903	26.6459304	10.15%
12/30/2011	3.9224267	1.3522810	2.5701457	24.0757847	10.15%
6/30/2012	4.3385247	1.2218461	3.1166786	20.9591061	10.15%
12/30/2012	4.9083562	1.0636746	3.8446815	17.1144245	10.15%
6/30/2013	3.0209270	0.8685570	2.1523699	14.9620546	10.15%
12/30/2013	6.5821701	0.7593243	5.8228458	9.1392088	10.15%
6/30/2014	6.5821701	0.4638148	6.1183553	3.0208535	10.15%
12/30/2014	3.1741618	0.1533083	3.0208534	0.0000000	10.15%
6/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%

LMC:NYPC-emloan.wr1

EXHIBIT B

ASSUMPTION AGREEMENT

TO: The Holders (as defined below) from time to time of the Notes (as defined below) of The First National Bank of Boston, not in its individual capacity, but solely as owner trustee under a Trust Agreement dated as of August 1, 1986 with Citizens Resources Company (in such capacity, the "Issuer") under the Trust Indenture, Mortgage, Security Agreement, and Assignment of Facility Lease (the "Indenture") dated as of August 1, 1986 between the Issuer and Chemical Bank, as trustee (the "Trustee").

The undersigned, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Obligor"), for the purpose of satisfying in part its obligation to make certain payments in respect of that certain Facility Lease dated as of August 1, 1986 between the Issuer and the Obligor (the "Facility Lease"), does hereby covenant and agree with the Holders (as defined in the Indenture) from time to time of the Notes (as defined in the Indenture) as follows:

SECTION 1. The Obligor does hereby agree to, and does hereby, assume unconditionally the payment of the principal of the Notes and of the interest and premium (if any) thereon, at the rates provided in the Notes, when and as the same shall become due and payable, whether at maturity or upon mandatory prepayment or upon declaration or otherwise, according to the terms of the Notes and of the Indenture. If any Initial Series Notes (as defined in the Indenture) are Outstanding (as defined in the Indenture), the Obligor agrees, upon surrender of the same to the Obligor for exchange at the Indenture Trustee's Office (as defined in the Indenture), together with the written request of the Holder of such Initial Series Note, or its attorney duly authorized in writing, in each case with signatures guaranteed, to exchange such Initial Series Note for a Bank Exchange Note in the same aggregate principal amount.

SECTION 2. The assumption herein contained shall be binding upon the Obligor, its successors and assigns, and shall remain in full force and effect irrespective of the power or authority of the Issuer to issue the Notes or to execute, acknowledge and deliver the Indenture or the validity of the Notes, or the Indenture, or of any defense whatsoever that the Issuer may or might have to the payment of the Notes (principal, interest or premium), or to the performance or observance of any of the provisions or conditions of the Indenture or any Note, or of the existence or continuance of the Issuer as a legal entity; nor shall said assumption be affected by the merger, consolidation, or other dissolution of the Issuer or the sale or other transfer of the property of the Issuer as an entirety, or substantially so, to any other person; nor shall the assumption be discharged or impaired by any act, failure or omission whatsoever on the part of any Holder of any Notes or the Trustee, including, among other such acts, failures and omissions, the following:

(a) any failure to present any Note for payment or to demand payment thereof, or to give to the Obligor notice of dishonor and non-payment of any Note when and as the same may become due and payable, or notice of any failure on the part of the Issuer to do any act or thing or to perform or keep any covenant or agreement by it to be done, kept or performed under the terms of Notes or the Indenture;

(b) any extension of the obligation of any Note, either indefinitely or for any period of time, or any other modification in the obligations under any Note or the Indenture or of the Issuer thereon or in connection therewith;

(c) any act or failure to act with regard to any Note or the Indenture or anything which might vary the risk of the Obligor; and

(d) any action taken under the Indenture and the Notes in the exercise of any right or power thereby conferred or any failure or omission on the part of the Trustee or the Holder of any Note to enforce any right or security given under the Indenture or any Note, or any waiver of any right or any failure or omission on the part of the Trustee or any Holder of any Note to enforce any right of any Holder of any Note against the Issuer;

provided, always, that the specific enumeration of the above mentioned acts, failures, waivers or omissions shall not be deemed to exclude any other acts, failures, waivers or omissions though not specifically mentioned herein, it being the purpose and intent of this Assumption Agreement that the obligation of the Obligor shall be absolute and unconditional to the extent herein specified and shall not be discharged, impaired or varied except by the payment of the principal of and interest on any Note and any premium thereon in case of prepayment, and then only to the extent of such payments.

SECTION 3. (a) Subject to the requirements of Section 10(b)(3)(ii) and the first sentence of Section 10(b)(3)(i) of the Participation Agreement and to the provisions of paragraph (b) of this Section, nothing contained in this Assumption Agreement shall prevent any consolidation or merger of the Obligor with or into any other corporation or corporations (whether or not affiliated with the Obligor), or successive consolidations or mergers in which the Obligor or its successor or successors shall be a party or parties, or shall prevent any sale, conveyance or lease of all or substantially all the property of the Obligor, to any other corporation authorized to acquire and operate the same; provided, however, and the Obligor hereby covenants and agrees, that upon any such consolidation, merger, sale, conveyance or lease, all obligations of the Obligor under this Assumption Agreement on or in respect of any Note, and the due and punctual performance and observance of all of the covenants and conditions of this Assumption Agreement to be performed by the Obligor, shall be expressly and duly assumed, by an agreement reasonably satisfactory in form and substance to the Trustee, executed and delivered by the corporation (if other than the Obligor) formed by such consolidation, or into which the Obligor shall have been merged, or by the corporation which shall have acquired such property.

(b) The Trustee, subject to applicable provisions of the Indenture, may rely upon an opinion of counsel to the Obligor as conclusive evidence that any such merger, consolidation, sale or conveyance complies with the provisions of this Section.

SECTION 4. The Obligor does hereby consent to all of the terms and conditions of each series of Notes and of the Indenture, and hereby waives any and all rights of notice of any fact or facts or circumstance or circumstances whatsoever and consents to any extension or extensions of time of any payment or payments, or of any other act or thing which any Holder or Holders of any Note or the Issuer may agree to consent to, either expressly, by acquiescence or otherwise, and hereby agrees not to claim or enforce any rights of subrogation or any other right or privilege which might otherwise arise on account of any payment made by it or act or thing done by it on account of or in accordance with its assumption herein contained, unless and until all of the Notes have been fully paid and discharged.

SECTION 5. The assumption herein expressed may be transferred or assigned at any time or from time to time and shall be considered to be transferred and assigned upon the transfer of any Note, whether with or without the consent of or notice to the Obligor or the Issuer. The Obligor hereby agrees to execute and deliver such instruments and to do such acts and things requested by the Trustee as shall be reasonably necessary to carry out and effectuate the purposes and intents of this Assumption Agreement. This Assumption Agreement may not be amended or modified in any respect without the prior written consent (evidenced as provided in the Indenture) of the Holders of not less than a majority in principal amount of the Notes Outstanding (as defined in the Indenture); provided, however, that without the written consent of the Holders of all of the Notes Outstanding, no such amendment or modification shall be effective which will change any of the provi-

sions of Sections 1, 2, 4 or 5 of this Assumption Agreement. The Obligor agrees to file with the Indenture Trustee a duplicate original of each such consent.

ARIZONA PUBLIC SERVICE COMPANY

By _____
Title:

ATTEST:

Title:

EXHIBIT C

FORM OF BANK EXCHANGE NOTE

ASSUMPTION AGREEMENT,
ALLONGE
AND NOVATION
OF
PROMISSORY NOTE

Date: _____

The undersigned ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Company"), in consideration of the release of the Company's obligations under that certain Facility Lease (the "Facility Lease"), dated as of August 1, 1986, between the Company as Lessee and The First National Bank of Boston, not in its individual capacity, but solely as owner trustee under a Trust Agreement dated as of August 1, 1986, with _____ (in such capacity, the "Issuer") as Lessor, hereby agrees personally, unconditionally and irrevocably to assume the outstanding obligations of the Issuer under the certain Note of the Issuer, issued by Issuer under that certain Trust Indenture, Mortgage, Security Agreement, and Assignment of Facility Lease dated as of August 1, 1986, between the Issuer and Chemical Bank, as trustee (the "Indenture"), to which Note this Assumption Agreement, Allonge and Novation of Promissory Note is affixed (the "Existing Note"); and, in order to induce the Holder (as such term is defined in the Indenture; all other capitalized terms used herein and not defined in Section 7 below or otherwise herein shall have the same respective meanings as defined in the Indenture) to consent to such release of the Company's obligations under the Facility Lease, which constitute part of the Lease Indenture Estate securing the Existing Note under the Indenture and to accept such assumption and the substitution of the Company for Issuer as obligor under the Existing Note, the Company hereby agrees to amend and modify the terms of the Existing Note, as set forth below. From and after the date of this Assumption Agreement, Allonge and Novation of Promissory Note, the terms and conditions set forth below (this "Note") shall amend and be substituted in their entirety for the terms of the Existing Note, and the obligations of the Company and the terms and conditions of this Note shall be as set forth herein, without reference to the Existing Note for any purpose.

THIS NOTE HAS NOT BEEN REGISTERED
UNDER THE SECURITIES ACT OF 1933 AND
MAY NOT BE TRANSFERRED, SOLD OR OFFERED
FOR SALE IN VIOLATION OF SUCH ACT.

RECOURSE PROMISSORY NOTE, INITIAL SERIES

No. _____ *

\$ _____ *

FOR VALUE RECEIVED, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Company"), hereby promises to pay to _____ * * ("Lender"), or registered assigns, the principal sum of dollars (\$ _____ *) (a "Loan"), such payment to be made in semiannual installments on June 30 and December 30 of each year beginning December 30, 1986, and ending December 30, 2015, each installment to be in an amount equal to the original principal amount of this Note multiplied by the percentage set forth opposite the applicable date on Schedule 1 attached hereto, provided that the remaining unpaid principal amount of this Note, together with all accrued but unpaid interest, shall in any and all cases, be due and payable on December 30, 2015; and to pay interest on such principal amount from time to time outstanding hereunder at the rates, and in the manner and at the times specified below. Both principal and interest are payable in lawful money of the United States of America ("Dollars") no later than 10:00 a.m. (Los Angeles time) on the day when due in funds immediately available to Bank of America National Trust and Savings Association ("Bank of America") acting in its capacity as agent for Lender ("Agent") at Bank of America Corporate Service Center-North, Department 1233, 1850 Gateway Boulevard, Concord, California 94520, Attention: Ms. Julie Hopkins (Re: Arizona Public Service Company), or at such other place as Agent shall designate, for the account of Lender. As between the Company and Lender, payments to Agent constitute payments to Lender.

This Note is one of the Notes referred to in, and is entitled to the collateral and other benefits of, the Indenture.

1. Interest Rate and Payment

Interest on the Loan shall be payable at a variable rate, per annum equal to two hundred percent (200%) of _____

* [As in original Note.]

** [As in original Note or, if applicable, the then current registered assign of such entity.]

the Reference Rate in effect from time to time as set forth below. "Reference Rate" shall mean the rate publicly announced from time to time by Bank of America in San Francisco, California, as its Reference Rate. Such rate is set by Bank of America based upon various factors, including Bank of America's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans; loans may be priced at, above, or below such Reference Rate. Any change in the Reference Rate shall take effect on the day specified in the public announcement of such change.

Interest on the Loan shall accrue from the date made until paid in full at the applicable rate in effect from time to time and shall be payable monthly, in arrears, on the first Business Day of each month.

2. Computations and Payment

All computations hereunder of interest on the Loan shall be computed on the basis of a year of 365 or 366 days, as the case may be. Whenever any payment to be made hereunder is stated to be due on a day that is not a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall be included in the computation of payment of interest. Funds received by the Agent after 10:00 a.m. (Los Angeles time) shall be deemed to have been received on the next succeeding Business Day.

3. Representations and Warranties

As an inducement to the Lender to accept this Note as aforesaid, the Company represents and warrants to the Lender as follows:

(a) Due Organization, Qualification, Etc. The Company is a corporation validly formed and existing and in good standing under the laws of the State of Arizona and is authorized to do business in the jurisdictions in which its ownership of property or conduct of business legally requires such authorization, and has full power, authority and legal right to own its properties and assets and to conduct its business as presently conducted or proposed to be conducted.

(b) Capacity. The Company has full power, authority and legal right to execute and deliver, and to perform and observe the provisions of this Note and has obtained all approvals and consents and completed all proceedings necessary to carry out the transactions contemplated hereby.

(c) Authority and Enforceability. The execution, delivery and performance by the Company of this Note and any

other instrument executed pursuant hereto, have been duly authorized by all necessary corporate action, and do not and will not require any approval of, notice to, or any action by, any Person (other than a Governmental Authority) and cannot and will not conflict with, result in any violation of, or constitute a default under, any provision of the articles of incorporation or bylaws of the Company or any agreement or other instrument binding upon or applicable to it, or any present law or governmental regulation or court decree or order applicable to it. This Note constitutes legal, valid and binding obligations of the Company enforceable against the Company in accordance with its terms, subject, as to enforcement only, to bankruptcy, insolvency, reorganization, moratorium or similar laws at the time in effect affecting the enforceability of the rights of creditors generally and to general principles of equity.

(d) Compliance with Other Instruments. The execution, delivery, and issuance of, and compliance with this Note will not result in a breach of any of the terms or conditions of, or result, except as contemplated by the Indenture, in the imposition of any lien, charge or encumbrance upon any properties of the Company pursuant to, or constitute a default (with due notice or lapse of time or both) or result in an occurrence of an event for which any holder or holders of Indebtedness may declare the same due and payable under, any indenture, agreement, order, judgment or instrument under which the Company is a party or by which the Company or its property may be bound or affected, or under its articles of incorporation or by-laws, and will not violate any provision of Applicable Law.

(e) Approvals. No authorization, registration with, consent or approval or other action by, and no notice to or filing with, any Governmental Authority or regulatory body is required for the due execution, delivery or performance by the Company of this Note, except for any such authorizations and approvals which have been duly obtained or made and are in full force and effect.

(f) Financial Information. The consolidated financial statements of the Company contained in the Company's Annual Report on Form 10-K for its latest full fiscal year (the "Form 10-K Report"), and in the Company's Form 10-Q Report for its latest full fiscal quarter (the "Form 10-Q Report"), filed with the Securities and Exchange Commission (the "SEC"), fairly present the consolidated financial position of the Company as at the dates indicated and the consolidated results of operations and sources of funds invested in utility plant and other plant for the periods therein specified, all in accordance with generally accepted accounting principles consistently applied, subject, in the case of the consolidated financial statements contained in the Form 10-Q Report, to the consolidation of

certain financial information and the omission of certain footnote disclosures, as permitted by the rules and regulations of the SEC, and to year-end audit adjustments. The Company represents and warrants that it knows of no such adjustments which would, if made on the date hereof, be material. Since the date of the Form 10-Q Report, and the Form 10-K Report, there has been no material adverse change in such consolidated financial position or operations.

(g) Litigation, Etc. Except as disclosed in the Form 10-K Report and the Form 10-Q Report, there are no actions, suits or proceedings (whether or not purportedly on behalf of the Company) pending, or to the knowledge of the Company threatened, against or affecting the Company, at law or in equity, before or by any Person, which, if adversely determined, would have a material adverse effect on the business, properties or the condition (financial or otherwise) of the Company. To the best of the Company's knowledge, (i) it is not in violation or default with respect to any applicable laws and/or regulations which materially affect the operations and/or condition (financial or otherwise) of the Company, (ii) it is not in violation or default with respect to any order, writ, injunction, demand or decree of any court or any Person the effect of which would be to materially affect the operations and/or conditions (financial or otherwise) of the Company, or (iii) it is not in violation or default (nor is there any waiver in effect which, if not in effect, would result in a violation or default) in any material respect under any agreement or instrument evidencing Debt, indenture, agreement or other instrument under which the Company is a party or may be bound, the effect of which would be to materially affect the operations and/or conditions (financial or otherwise) of the Company.

(h) Security Interests. The Lien of the Indenture constitutes a valid first priority perfected Lien upon and assignment and pledge of the property described therein as security for the payment and performance of the Company's obligations under and with respect to this Note, subject to no prior security or interest, claim, or right.

(i) No Default. To the best of the Company's knowledge, no Event of Default, nor any event which, with the lapse of time or the giving of notice, or both, would constitute an Event of Default, has occurred and is continuing.

(j) Title to the Undivided Interest; Security Interest. As of the date of this Assumption Agreement, Allonge and Novation to Promissory Note, the Company has good and marketable title to the Undivided Interest, including the related Generation Entitlement Share, free and clear of all Liens, except Permitted Liens, and to the Retained

Assets. All filings and recordings necessary or advisable to perfect and continue the Lien of the Indenture on the Lease Indenture Estate and to establish and maintain the continuing first priority of such Lien have been duly made.

4. Affirmative Covenants

Until payment in full of this Note, the Company agrees that:

(a) Fixed Charge Ratio. Maintain at all times a Fixed Charge Ratio of at least 2 to 1. "Fixed Charge Ratio" shall mean at any time the ratio of (A) the sum of (x) the consolidated net income of the Company and its subsidiaries for the twelve month period ending with the last month for which the Company has prepared a consolidated income statement, which period shall in no event end earlier than the last day of the month two months prior to the time of the calculation of the Fixed Charge Ratio (the "Twelve Month Period") plus (y) all income taxes deducted in determining said consolidated net income plus (z) the sum of (i) all interest expense in respect of Indebtedness deducted in determining said consolidated net income, (ii) all interest expense in respect of Funded Indebtedness being incurred at the time of the calculation of the Fixed Charge Ratio that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate and (iii) all interest expense in respect of Indebtedness other than Funded Indebtedness (I) incurred at any time subsequent to the Twelve Month Period and outstanding at the time of the calculation of the Fixed Charge Ratio and (II) being incurred at the time of the calculation of the Fixed Charge Ratio, that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate (the aggregate interest expense described in this clause (z) being referred to as the "Interest Expense") to (B) Interest Expense for such period.

(b) Financial Information. The Company will furnish to the Agent: (i) as soon as possible, and in any event within ten days after the Company knows or has reason to know of the occurrence of each Event of Default or each event which, with the giving of notice or lapse of time, or both, would constitute an Event of Default, continuing on the date of such statement, a statement of the chief financial officer (or in his absence, a principal financial officer) of the Company setting forth details of such Event of Default or event and the action which the Company proposes to take with respect thereto; (ii) as soon as possible, and in any event within fifteen days after filing each of the Company's Reports on Form 8-K with the Securities and Exchange Commission, a copy of each of such reports; (iii) as soon as available and in any event within

30 days after filing of each of the Company's Reports on Form 10-Q with the Securities and Exchange Commission, a copy of each of such reports together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Event of Default, or event which, with notice or lapse of time or both, would constitute an Event of Default, has occurred and is continuing or, if an Event of Default or such event has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereof and (y) setting forth, and certifying to the accuracy of, a current calculation of the Fixed Charge Ratio required under Section 4(a) hereof; (iv) as soon as available and in any event within 30 days after filing of each of the Company's Annual Reports on Form 10-K with the Securities and Exchange Commission, a copy of each of such reports, together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Event of Default, or event which, with notice or lapse of time or both, would constitute an Event of Default, has occurred and is continuing or, if an Event of Default or such event has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth, and certifying to the accuracy of, a current calculation of the Fixed Charge Ratio required under Section 4(a) hereof; and (vii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the Company as the Agent may from time to time reasonably request in writing.

(c) Insurance. The Company shall maintain insurance with responsible and reputable insurance entities or associations or through its own program of self insurance in such amounts and covering such risks as is usually carried by entities engaged in similar businesses and owning similar properties in the same general areas in which the Company operates.

(d) Other Debt. The Company will promptly pay and discharge any and all Indebtedness, liens, charges, all taxes, assessments and governmental charges or levies imposed upon it or upon its income or profits, or upon any of its properties prior to the date on which penalties accrue thereon, and lawful claims which, if unpaid, might become a lien or charge upon the property of the Company, the effect of which would materially affect the operations and/or conditions (financial or otherwise) of the Company, except such as may in good faith be contested or disputed, or for which arrangements for deferred payment have been made, provided appropriate reserves are maintained to the reasonable satisfaction of the Agent.

(e) Maintenance of Existence. The Company will cause to be done at all times all things necessary to maintain the corporate existence of the Company.

(f) Conduct of Business. The Company will do or cause to be done all things necessary to preserve and keep in full force and effect its material franchises; provided, however, that the Company may discontinue or permit the discontinuance of any material franchise if (x) its board of directors shall determine that such discontinuance is necessary or desirable in the conduct of its business and does not materially and adversely affect or diminish any right of the Lender hereunder or (y) the Company continues to provide electric service to the area covered by such material franchise to the substantially same extent and on substantially the same terms and conditions as provided prior to such discontinuance pending the renegotiation or renewal thereof.

(g) Expenses. The Company will pay all reasonable out-of-pocket expenses of the Agent (including, but not limited to, fees and disbursements of the Agent's independent and in-house counsel) incident to the administration of the obligations evidenced by this Note, including the fees and charges of Agent, any amendments or waivers to this Note, the protection of the rights of the Lender or Agent under this Note or the Indenture and the enforcement of payment of this Note, whether by judicial proceedings or otherwise. The obligations of the Company under this Section 4(g) shall survive payment and cancellation of this Note.

(h) Books and Records. The Company will at all times keep books of record and account reflecting its business affairs and transactions in which proper entries will be made of said business affairs and its transactions in accordance with generally accepted accounting principles.

(i) Inspection. At any reasonable time and from time to time, permit Lender or any agents or representatives thereof to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its subsidiaries with any of their respective officers or directors; provided, however, that the Company reserves the right to restrict access to any of its generating facilities in accordance with reasonably adopted procedures relating to safety and security; and provided, further, that, Subsection (g) above notwithstanding, the costs and expenses incurred by Lender or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions occurring or made prior to the occurrence of an Event of Default shall be for the account of Lender. Lender

agrees to use reasonable efforts to ensure that any information concerning the Company or any of its subsidiaries obtained by Lender pursuant to this Subsection which is not contained in a report or other document filed with the Securities and Exchange Commission, distributed by the Company to its shareholders or otherwise available to the public generally will, to the extent permitted by law and except as may be required by valid subpoena or in the normal course of Lender's business operations be treated confidentially by Lender and will not be distributed or otherwise made available by Lender to any person or entity, other than the Agent or the Lender's or the Agent's employees, authorized agents or representatives.

(j) Operation and Maintenance. The Company will operate and maintain Unit 2 in accordance with the terms and provisions of Section 8(a) of the Facility Lease, as such Section 8(a) was in effect immediately following the execution and delivery of the Facility Lease by the Company, and notwithstanding any subsequent amendment, expiration or termination of the Facility Lease. Such Section 8(a) is incorporated herein by reference.

(k) Maintenance of Equity. Maintain at all times common stock equity, as calculated in accordance with generally accepted accounting principles consistently applied and set forth from time to time in the consolidated balance sheets of the Company and its subsidiaries, of at least \$1.4 billion.

5. Events of Default

If one or more of the following described events shall occur ("Event of Default"):

(a) The Company shall fail to pay in full any principal hereof or interest hereon when the same becomes due; or

(b) The Company shall fail to perform or observe any of the provisions contained in any other Section of this Note and such failure shall continue for more than thirty (30) days after notice to the Company from the Agent or the Lender of such failure; or

(c) Any representation or warranty made in writing by or on behalf of the Company herein or pursuant hereto, or otherwise in connection with the transactions contemplated hereby or any report, certificate, financial or other instrument furnished in connection with this Note, shall prove to have been false or incorrect in any

material respect, or omits to state a material fact required to be stated therein in order to make the statements contained therein, in the light of the circumstances under which made, not misleading, on the date as of which made; or

(d) The Company shall cause a default as defined in any evidence of Indebtedness of the Company in aggregate principal amount in excess of \$20,000,000, or under any indenture, agreement or other instrument under which the same may be issued and, as a result thereof, the holder of such evidence of Indebtedness shall accelerate the maturity thereof; or

(e) The Company shall commence a voluntary case or other proceeding seeking liquidation, reorganization or other relief with respect to itself or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, or shall consent to any such relief or to the appointment of or taking of possession by any such official in an involuntary case or other proceeding commenced against it, or shall make a general assignment for the benefit of creditors, or shall take any corporate action to authorize any of the foregoing; or an involuntary case or other proceeding shall be commenced against the Company seeking liquidation, reorganization or other relief with respect to it or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, and such involuntary case or other proceeding shall remain undismissed or unstayed for a period of 60 days consecutive days; or

(f) final judgment for the payment of money in excess of \$5,000,000 shall be rendered against the Company and the Company shall not have discharged the same or provided for its discharge in accordance with its terms or bonded the same or procured a stay of execution thereof within 60 days from the entry thereof;

THEN, or at any time thereafter:

(1) Where the Company is in default under the provisions of Section 5(e), the entire unpaid principal

amount of this Note, all interest accrued and unpaid thereon and all other amounts payable hereunder shall automatically become and be forthwith due and payable, without presentment, demand, protest or notice of any kind, all of which are hereby expressly waived by the Company;

(2) In any other case referred to in this Section 5, the Holder may, at its option, by written notice to the Company, declare the entire unpaid principal amount of this Note, all interest accrued and unpaid thereon and all other amounts payable hereunder to be forthwith due and payable, whereupon the same shall become immediately due and payable, without presentment, demand, protest or further notice of any kind, all of which are hereby expressly waived by the Company.

In the case of either (1) or (2) above, the Holder may immediately and without expiration of any period of grace, enforce payment of all Obligations of the Company to it under this Note, and with the Agent and through the Indenture Trustee may exercise all available rights and remedies under the Indenture and Applicable Law.

6. Definitions

As used herein, and unless otherwise defined herein, the following terms shall have the following respective meanings:

"Funded Indebtedness" means the Indebtedness evidenced by this Note and all other Indebtedness which matures more than one year from the date of its creation or matures within one year from such date but is renewable or extendible, at the option of the Company, to a date more than one year from such date or arises under a revolving credit or similar agreement which obligates the lender or lenders to extend credit during a period of more than one year from such date including, without limitation, all amounts of Funded Indebtedness required to be paid or prepaid within one year from the date of its creation.

"Guaranteed Indebtedness" of any Person means all Indebtedness referred to in clause (i), (ii) or (iii) of the definition of "Indebtedness" in this Section guaranteed directly or indirectly in any manner by such Person, or in effect guaranteed directly or indirectly by such Person through an agreement (i) to pay or purchase such Indebtedness or to advance or supply funds for the payment or purchase of such Indebtedness, or (ii) to purchase, sell or lease (as lessee or lessor) property, or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such Indebtedness or to assure the holder of such Indebtedness against loss, or (iii) to supply funds to or in any other manner invest in the debtor (including

any agreement to pay for property or services irrespective of whether or not such property is received or such services are rendered), or (iv) otherwise to assure a creditor against loss.

"Imputed Rate" means, in respect of Indebtedness, the actual initial rate of interest per annum to be paid by a Person with respect to such Indebtedness.

"Indebtedness" of any Person means (i) all indebtedness of such person for borrowed money or for the deferred purchase price of property or services, (ii) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property acquired by such Person (even though the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property), (iii) all obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, recorded as capital leases in respect of which such Person is liable as lessee, (iv) all Guaranteed Indebtedness, and (v) all Indebtedness referred to in clause (i), (ii) or (iii) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any lien, security interest or other charge or encumbrance upon or in property (including, without limitation, accounts and contracts rights) owned by such Person, even though such person has not assumed or become liable for the payment of such Indebtedness.

"Obligations" shall mean and include all loans, advances, debts, liabilities, obligations, letters of credit or acceptance transactions, trust receipt transactions, or any other financial accommodations, howsoever arising, owing by the Company to, or on behalf of, the Lender of every kind and description (whether or not evidenced by any note or other instrument and whether or not for the payment of money), direct or indirect, absolute or contingent, due or to become due, now existing or hereafter arising pursuant to the terms of this Note, including, without limitation, all interest, fees, charges, expenses, attorneys' fees and accountants' fees chargeable to the Company or incurred by the Lender or Agent in connection with its dealings with the Company.

7. Miscellaneous

(a) No Waiver. No failure to exercise, and no delay in exercising any right, power or remedy hereunder or under any document delivered pursuant hereto shall impair any right, power or remedy which the Lender may have, nor shall any such delay be construed to be a waiver of any of such rights, powers or remedies, or an acquiescence in any

breach or default under this Note or any document delivered pursuant hereto, nor shall any waiver of any breach or default of the Company hereunder be deemed a waiver of any default or breach subsequently occurring. The rights and remedies herein specified are cumulative and not exclusive of any rights or remedies which the Lender or Agent would otherwise have.

(b) Notices. All notices, requests, consents and demands hereunder shall be in writing and shall be effective when duly deposited in the mails, registered mail postage prepaid, or delivered to the telegraph company or transmitted by telex, addressed to the respective party at the address set forth below, except that notices to the Lender or Agent pursuant to this Section 8(b) shall not be effective until received.

Company: Arizona Public Service Company
411 North Central Avenue
P.O. Box 53999
Phoenix, Arizona 85072-3999
Attn: Secretary

Holder or Agent: Bank of America National Trust
and Savings Association
555 S. Flower Street
Los Angeles, California 90071
Attn: Mr. Gregory House

With a copy to:

Bank of America National Trust
and Savings Association
Bank of America Corporate
Service Center - North
Department 1233
1850 Gateway Boulevard
Concord, California 94520
Attn: Ms. Julie Hopkins
(Re: Arizona Public Service
Company)

Any of the parties hereto may change their respective address by notice in writing given to the other parties to this Agreement.

(c) Termination. This Note shall terminate only when all Obligations of the Company incurred hereunder and evidenced hereby shall have been discharged in full.

(d) Severability of Provisions. In case any one or more of the provisions contained in this Note should be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining

provisions contained herein shall not in any way be affected or impaired thereby.

(e) Recourse Note. Notwithstanding anything to the contrary contained in the Existing Note as previously in effect prior to this Assumption Agreement, Allonge and Novation of Promissory Note and notwithstanding anything to the contrary contained in the Lease or in the Indenture or in any other agreement, the Company shall be personally liable to the Holder of this Note for any and all amounts payable under this Note or the Indenture.

IN WITNESS WHEREOF, the Company has caused this Assumption Agreement, Allonge and Novation of Promissory Note to be duly executed as of the day and year first above written.

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona Corporation

By: _____

Name: _____

Title: _____

This Note is one of the series of Notes referred to therein and in the within-mentioned Indenture.

CHEMICAL BANK
As Indenture Trustee,

By _____
Authorized Officer

Schedule 1 - Amortization of the
Bank Exchange Note

Amounts Stated as a percent of Original Principal

Original Principal Amount as a percent of Facility Cost : 78.3117544%

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
12/30/1986	2.9333333	2.9333333	0.0000000	100.0000000	8.00%
6/30/1987	5.3854120	5.0750000	0.3104120	99.6895880	10.15%
12/30/1987	5.3854120	5.0592466	0.3261654	99.3634226	10.15%
6/30/1988	5.3854120	5.0426937	0.3427183	99.0207044	10.15%
12/30/1988	5.3854120	5.0253007	0.3601112	98.6605931	10.15%
6/30/1989	5.3854120	5.0070251	0.3783869	98.2822063	10.15%
12/30/1989	5.3854120	4.9878220	0.3975900	97.8846163	10.15%
6/30/1990	5.3854120	4.9676443	0.4177677	97.4668486	10.15%
12/30/1990	5.3854120	4.9464426	0.4389694	97.0278792	10.15%
6/30/1991	5.3854120	4.9241649	0.4612471	96.5666320	10.15%
12/30/1991	5.3854120	4.9007566	0.4846554	96.0819766	10.15%
6/30/1992	5.3854120	4.8761603	0.5092517	95.5727250	10.15%
12/30/1992	5.3854120	4.8503158	0.5350962	95.0376288	10.15%
6/30/1993	5.3854120	4.8231597	0.5622523	94.4753765	10.15%
12/30/1993	5.3854120	4.7946254	0.5907866	93.8845899	10.15%
6/30/1994	5.3854120	4.7646429	0.6207690	93.2638208	10.15%
12/30/1994	5.3854120	4.7331389	0.6522731	92.6115478	10.15%
6/30/1995	5.3854120	4.7000360	0.6853759	91.9261718	10.15%
12/30/1995	5.3854120	4.6652532	0.7201588	91.2060131	10.15%
6/30/1996	5.3854120	4.6287052	0.7567068	90.4493063	10.15%
12/30/1996	5.3854120	4.5903023	0.7951097	89.6541966	10.15%
6/30/1997	5.3854120	4.5499505	0.8354615	88.8187351	10.15%
12/30/1997	6.5821701	4.5075508	2.0746193	86.7441158	10.15%
6/30/1998	6.5821701	4.4022639	2.1799062	84.5642095	10.15%
12/30/1998	6.5821701	4.2916336	2.2905365	82.2736731	10.15%
6/30/1999	6.5821701	4.1753889	2.4067812	79.8668919	10.15%
12/30/1999	6.5821701	4.0532448	2.5289254	77.3379665	10.15%
6/30/2000	6.5821701	3.9249018	2.6572683	74.6806982	10.15%
12/30/2000	6.5821701	3.7900454	2.7921247	71.8885735	10.15%
6/30/2001	5.9814313	3.6483451	2.3330862	69.5554873	10.15%
12/30/2001	5.0408577	3.5299410	1.5109167	68.0445706	10.15%
6/30/2002	5.2799583	3.4532620	1.8266964	66.2178742	10.15%
12/30/2002	4.9521294	3.3605571	1.5915723	64.6263019	10.15%
6/30/2003	5.2067660	3.2797848	1.9269812	62.6993207	10.15%
12/30/2003	4.8605733	3.1819905	1.6785827	61.0207380	10.15%
6/30/2004	5.1295660	3.0968025	2.0327636	59.9879744	10.15%
12/30/2004	4.7640002	2.9936397	1.7703605	57.2176139	10.15%
6/30/2005	5.0481360	2.9037939	2.1443421	55.0732718	10.15%
12/30/2005	4.6621356	2.7949685	1.8671670	53.2061048	10.15%
6/30/2006	4.9622442	2.7002098	2.2620344	50.9440704	10.15%
12/30/2006	4.5546895	2.5854116	1.9692779	48.9747925	10.15%
6/30/2007	4.8716461	2.4854707	2.3861754	46.5886172	10.15%
12/30/2007	4.4413560	2.3643723	2.0769837	44.5116335	10.15%
6/30/2008	4.7760838	2.2589654	2.5171184	41.9945151	10.15%
12/30/2008	4.3218127	2.1312216	2.1905911	39.8039239	10.15%

Schedule 1 - Amortization of the
Bank Exchange Note

Date	Debt Service	Interest	Principal	Principal Balance	Interest Rate
6/30/2009	4.6752854	2.0200491	2.6552362	37.1486877	10.15%
12/30/2009	4.1957193	1.8852959	2.3104234	34.8382643	10.15%
6/30/2010	4.5689639	1.7680419	2.8009220	32.0373423	10.15%
12/30/2010	4.0627168	1.6258951	2.4368217	29.6005207	10.15%
6/30/2011	4.4568167	1.5022264	2.9545903	26.6459304	10.15%
12/30/2011	3.9224267	1.3522810	2.5701457	24.0757847	10.15%
6/30/2012	4.3385247	1.2218461	3.1166786	20.9591061	10.15%
12/30/2012	4.9083562	1.0636746	3.8446815	17.1144245	10.15%
6/30/2013	3.0209270	0.8685570	2.1523699	14.9620546	10.15%
12/30/2013	6.5821701	0.7593243	5.8228458	9.1392088	10.15%
6/30/2014	6.5821701	0.4638148	6.1183553	3.0208535	10.15%
12/30/2014	3.1741618	0.1533083	3.0208534	0.0000000	10.15%
6/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%
12/30/2015	0.0000000	0.0000000	0.0000000	0.0000000	10.15%

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1. The effectiveness of Section 6.11 of the Indenture is suspended in its entirety and the following provisions shall apply in lieu thereof:

Except as otherwise provided in this Section, but notwithstanding any contrary or inconsistent provision of the Indenture, subject, however, to Section 10.2 of the Indenture, (a) at all times prior to the occurrence of an Indenture Event of Default, the Owner Trustee shall retain, to the exclusion of the Indenture Trustee, all rights of the Owner Trustee to exercise any election or option or to make any decision or determination or to give or receive any notice, consent, waiver or approval or to take any other action under or in respect of the Facility Lease, as well as all rights, powers and remedies on the part of the Owner Trustee, whether arising under the Facility Lease or by statute or at law or in equity or otherwise, arising out of any Default or Event of Default; provided, however, that, except insofar as it relates to Excepted Payments or Excepted Rights to which it is entitled, the Owner Trustee shall not, except with the prior written consent of the Indenture Trustee, agree or consent to any amendment to, or any waiver, discharge or termination of, or give any consent under any term or provision of Sections 2(c), 3(g), 4, 7, 8(f) (iv), 9(i), 11, 15(i) (x), (i) (y), (vii) and (x) and the provisions relating to the redemption of Notes in Section 14 of the Facility Lease and any amendment to Section 16 of the Facility Lease; and, provided, further, that the Owner Trustee shall, in any event, observe and perform its covenants contained in clause (iv) of Section 6.1 of the Indenture; and, provided, further, that during the continuance of any Event of Default the Owner Trustee shall promptly provide the Indenture Trustee with notice or copies of any notice, consent, waiver or approval given or received and any other action taken under clause (a); (b) upon and for a period not to exceed 60 days after the occurrence of an Indenture Event of Default described in clause (y) of paragraph (a) of Section 6.3 of the Indenture, (i) the Owner Trustee and the Agent shall consult and cooperate in good faith, and, the Owner Trustee and the Indenture Trustee shall act or refrain from acting concurrently, in exercising all rights, powers and remedies of each arising under the Facility Lease and the Indenture, respectively, in all

instances with a view to protecting and preserving the respective rights and remedies of the Owner Trustee and the Holders of the Notes under the Facility Lease and the Indenture and, to the extent reasonably practicable, maximizing the prospects of recovery; without limiting the generality of the foregoing, the Owner Trustee and Indenture Trustee shall jointly exercise all rights enumerated in clause (a) above; (c) upon and at all times after the occurrence of an Indenture Event of Default described in clause (x) (ii) of paragraph (a) of Section 6.3 of the Indenture or under the circumstances described in clause (x) (i) of such paragraph, the Indenture Trustee shall have, and may freely exercise, to the exclusion of the Owner Trustee, all rights enumerated in clause (a) above and under the Indenture; provided however, that nothing in this Section shall be deemed or construed to require the Owner Trustee or Indenture Trustee to act or refrain from acting in violation of Applicable Law, nor shall the exercise of any rights, powers and remedies result, without the consent of the Owner Trustee, in the transfer of any part of the Lease Indenture Estate to a Person other than a Transferee as defined in the ANPP Participation Agreement. Notwithstanding any provision of this Section to the contrary (other than the proviso to the preceding sentence), the Indenture Trustee may sell the Lease Indenture Estate in foreclosure or similar proceedings if (i) such sale occurs prior to or simultaneously with termination of the Facility Lease, (ii) the Indenture Trustee shall by written notice have offered to sell its right, title and interest in and to the Lease Indenture Estate to the Owner Trustee at a stated price determined by the Indenture Trustee (the "Stated Price") and (iii) Owner Trustee shall not have notified the Indenture Trustee in writing within 60 days after receipt of such notice of its irrevocable election to purchase the Lease Indenture Estate at the Stated Price on a date within 60 days after the date of such notice of election. If the Owner Trustee shall fail timely to elect so to purchase the Lease Indenture Estate, the Indenture Trustee shall be free to foreclose and sell the Lease Indenture Estate to any Person (other than the Indenture Trustee, Agent or any Holder(s) or Affiliates of any thereof) at a price no lower than the Stated Price at any time within 180 days after such failure to deliver such notice of election. Upon payment by the Owner Trustee to the Indenture Trustee of the Stated Price, the Indenture Trustee shall transfer to the Owner Trustee, free from the lien of this Indenture, all of the Indenture Trustee's right, title and interest in and to the Lease Indenture Estate. At any time after the

termination of the Facility Lease or expiration of the 180 day period described in the second preceding sentence, the Indenture Trustee may exercise any right under Applicable Law to dispose of any interest in the Lease Indenture Estate, free of any right of the Owner Trustee to purchase the same.

2. Notwithstanding anything to the contrary contained in Section 6.8(c) of the Indenture, the Owner Trustee shall not terminate the Facility Lease or arrange for the substitution of another Person as lessee under a new lease without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

3. Notwithstanding anything to the contrary contained in Section 2.3 of the Indenture, there shall be no release of all or any portion of the Lease Indenture Estate from the security or other interest created by Section 2.1 of the Indenture without the prior written consent of the Agent, which consent will not be unreasonably withheld or delayed.

4. If at the time any Special Transfer is affected, the Lessee shall not have assumed the obligations under the Initial Series Notes, any subsequent breach by Lessee of its covenants contained in Section 10(b)(3)(vii) of the Participation Agreement shall be an event of Default and an Indenture Event of Default.

5. Any failure by the Owner Trustee to pay the Initial Series Notes in full when and as required by Section 13(d) or Section 14(b) or 14(c) shall be an Indenture Event of Default.

6. The provisions of this Annex A shall prevail to the extent they are inconsistent with or contrary to the provisions of any of the Transaction Documents.

7. The provisions of this Annex A shall remain in full force and effect until the full payment of all principal of and premium, if any, and interest on the Initial Series Notes.

ARIZONA PUBLIC SERVICE COMPANY

Sale and Leaseback of an Undivided
Interest in Palo Verde Nuclear Generating
Station Unit 2

Emerson Capital Corporation

TRANSACTION DOCUMENTS

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Amendment No. 1 to Participation Agreement	2
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Trust Agreement	4
Facility Lease	5
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When Recorded, Return to: David A. Sprentall
SNELL & WILMER
3100 Valley Bank Center
Phoenix, Arizona 85073

SUPPLEMENTAL INDENTURE NO. 1

Dated as of November 1, 1986

To

TRUST INDENTURE, MORTGAGE, SECURITY AGREEMENT AND ASSIGNMENT OF
FACILITY LEASE

Dated as of August 1, 1986

between

THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement dated as of August 1, 1986 with Emerson Capital Corporation (assignee of Emerson Finance Co.)

and

CHEMICAL BANK,
as Indenture Trustee

Original Indenture Recorded on August 18, 1986, as Instrument No. 86-439440 in Maricopa County, Arizona Recorder's Office.

SUPPLEMENTAL INDENTURE No. 1 dated as of November 1, 1986 to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986, between THE FIRST NATIONAL BANK OF BOSTON, a national banking association (FNB), not in its individual capacity, but solely as Owner Trustee (the Owner Trustee) under a Trust Agreement dated as of August 1, 1986, between FNB, whose address is 100 Federal Street, Boston, Massachusetts 02110, with Emerson Capital Corporation (assignee of Emerson Finance Co.), a Delaware corporation, and CHEMICAL BANK, a New York banking corporation (the Indenture Trustee), whose address is 55 Water Street, New York, New York 10041.

W I T N E S S E T H:

WHEREAS, the Owner Trustee and the Indenture Trustee have entered into a Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986 (the Indenture) pursuant to which the Owner Trustee has issued the Initial Series Notes;

WHEREAS, Section 3.5(1) of the Indenture provides, among other things, that the Initial Series Notes may be refunded with Refunding Notes;

WHEREAS, Section 3.5(4) of the Indenture provides, among other things, that the Owner Trustee and the Indenture Trustee may enter into indentures supplemental to the Indenture for, among other things, the purpose of establishing the terms, conditions and designations of Refunding Notes;

WHEREAS, the Owner Trustee desires to issue Refunding Notes to effect a refunding of the Initial Series Notes and to enter into this Supplemental Indenture No. 1 to establish the terms, conditions and designations of such Refunding Notes; and

WHEREAS, Section 10.1(viii) of the Indenture provides that, without the consent of Holders of the Notes Outstanding, the Indenture Trustee may, with the written consent of the Owner Trustee, from time to time and at any time execute a supplement to the Indenture in order to evidence the issuance of, and to provide the terms of, Refunding Notes;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Definitions.

For purposes hereof, capitalized terms used herein and not otherwise defined herein shall have the meanings assigned to such terms in Appendix A attached hereto.

SECTION 2. Terms, Conditions and Designations of the Refunding Notes.

(a) The Refunding Notes

There is hereby created and established a separate series of Notes of the Owner Trustee designated "Nonrecourse Promissory Notes, Refunding Series 1986", herein referred to as the Refunding Notes. The Refunding Notes shall be payable as to principal and bear interest on the principal amount thereof as follows:

<u>Refunding Note Due</u>	<u>Interest Rate</u>	<u>Original Principal Amount</u>
December 30, 1998	9.00%	\$ 20,956,000
June 30, 2015	10.45	139,044,000
		<u>\$160,000,000</u>

The Refunding Note due December 30, 1998 shall be substantially in the form of Exhibit A-1 to this Supplemental Indenture No. 1. The Refunding Note due June 30, 2015 shall be substantially in the form of Exhibit A-2 to this Supplemental Indenture No. 1. Each Refunding Note shall bear interest on the principal amount thereof from time to time Outstanding from the Issue Date designated thereon until paid at the rate of interest set forth therein, which interest shall be payable on December 30, 1986 and on each June 30 and December 30 thereafter to and including the maturity date thereof, unless paid in full prior to such date as provided herein and in such Refunding Note. The principal amount of each Refunding Note shall be payable on the dates and in the amounts as set forth in Schedule 1 attached thereto, as such Schedule may be adjusted from time to time in accordance with the terms hereof and of such Refunding Note. Installments of interest on and principal of (and premium, if any, on) each Refunding Note shall be due and payable on the payment dates specified in Schedule 1 attached thereto.

Each Refunding Note shall be subject to prepayment as set forth in such Refunding Note.

(b). Certain Adjustments to Amortization Schedules.

The schedule of principal amortization attached to each Refunding Note may be adjusted at the discretion of the Owner Trustee on one occasion prior to June 30, 1989; provided, however, that no such adjustment shall be made by the Owner Trustee which will increase or reduce the average life of such Refunding Note (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than six months; provided further, however, such adjustment may be made only in connection with an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease. If the Owner Trustee shall elect to make the foregoing adjustment, the Owner Trustee shall deliver to the Indenture Trustee and to the Lessee at least 60 days prior to the first payment date (specified on the schedule to such Refunding Note) proposed to be affected by such adjustment, a certificate of the Owner Trustee (x) stating that the Owner Trustee has elected to make such adjustment, (y) setting forth the revised schedule of principal amortization for such Refunding Note and (z) attaching calculations showing that the average life of such Refunding Note will not be reduced or increased except as permitted by this paragraph (b). The Indenture Trustee may rely on such Owner Trustee certificate and shall have no duty with respect to the calculations referred to in the foregoing clause (z).

SECTION 3. Amendments to Indenture.

(a) The Table of Contents to the Indenture is amended hereby to delete the reference to Schedule I.

(b) The fourth and fifth WHEREAS clauses of the Indenture are amended hereby in their entirety to read as follows:

"WHEREAS, in the circumstances contemplated by Sections 2(d), 2(e) and 2(f) of the Participation Agreement, the Owner Trustee may desire to issue Refunding Notes (together with any other Notes issued hereunder other than the Initial Series Notes, the Additional Notes) or to increase the principal amount of the Outstanding Refunding Notes or to change the amortization of either or both thereof;

WHEREAS, in order to finance the Supplemental Financing Amount of Capital Improvements and to refund notes of any series previously issued, the Owner Trustee may desire to issue Additional Notes hereunder secured on a pari passu basis with other Notes Outstanding from time to time;"

(c) Section 2.3 of the Indenture is amended hereby by replacing the capitalized term "Lien" in the first sentence of Section 2.3 with the clause "security and other interests" and by replacing the phrase "opinion relates" in the first sentence of Section 2.3 with the phrase "opinion relate".

(d) Section 3.5(1) of the Indenture is amended hereby by inserting the term "Extraordinary Casualty Value," after the term "Casualty Value," in the first sentence of Section 3.5(1).

(e) Section 3.5(2) of the Indenture is amended hereby by replacing the clause "the date of issuance" in the first sentence of Section 3.5(2) with the clause "the proposed date of issuance".

(f) Section 3.5(4)(b)(iv) of the Indenture is amended hereby by inserting the term "Extraordinary Casualty Value" after the term "Casualty Value" in Section 3.5(4)(b)(iv).

(g) Section 3.9(b) of the Indenture is amended hereby by inserting the clause "or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement" after the term "Cure Option" in the first sentence of Section 3.9(b).

(h) Section 3.9(c) of the Indenture is amended hereby by inserting the clause "or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement" before the period at the end of Section 3.9(c).

(i) Section 3.12 of the Indenture is amended hereby by inserting the following immediately after the first semicolon in Section 3.12:

"provided, however, that no such adjustment shall be made by the Owner Trustee which will increase or reduce the average life of such Refunding Notes (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than six months;"

and replacing the phrase "provided, however" in Section 3.12 with the phrase "provided further, however".

(j) Section 5.2 of the Indenture is amended hereby by amending the first and second sentence of Section 5.2 in their entirety as follows:

"If an Event of Loss or Deemed Loss Event shall occur or the Lessee shall exercise the Cure Option or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement, any amounts of Casualty Value, Special Casualty Value, Extraordinary Casualty Value or Fair Market Sales Value received or held by the Indenture Trustee in respect of such Event of Loss or Deemed Loss Event or exercise of the Cure Option or the purchase option referred to in Section 10(b)(3)(ix) of the Participation Agreement shall, except as otherwise provided in Section 5.3, be distributed forthwith to the Equity Participant. If the Lessee or Owner Trustee, as the case may be, shall exercise its option to terminate the Facility Lease pursuant to Section 14 thereof, then there shall be prepaid, on the Obsolescence Redemption Date, the unpaid principal amount of all Notes and all accrued but unpaid interest thereon to the date of such prepayment, to the extent that there shall have been paid or provision made for payment of the amounts due on the Notes on the Obsolescence Redemption Date."

(k) Section 6.2(g) of the Indenture is amended hereby by replacing the reference "7(b)(i)" in Section 6.2(g) with the reference "7(b)(1)".

(l) Section 6.4(e) of the Indenture is amended hereby by replacing the term "ANPP Project Agreement" in Section 6.4(e) with the term "ANPP Project Agreements".

(m) Section 6.8(a) of the Indenture is amended hereby by replacing the clause "on the date such Basic Rent was payable" in Section 6.8(a) with the clause "on the date such Rent was payable".

(n) Section 10.2 of the Indenture is amended hereby by deleting the following in Section 10.2 in its entirety:

"Notwithstanding the foregoing, the Indenture Trustee shall, upon receipt of a written instruction from the Lessee and the Owner Trustee, consent to an amendment of any definitions contained in or appended to this Indenture which are being changed pursuant to the amendments, if any, referred to in Section 10(b)(3)(xii) of the Participation Agreement."

(o) Section 10.3 of the Indenture is amended hereby by replacing the term "the Facility Lease" in Section 10.3 with the term "any Granting Clause Document".

(p) Appendix A to the Indenture is hereby deleted and replaced by Appendix A attached hereto.

SECTION 4. Miscellaneous.

(a) Execution.

This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(b) Execution as Supplemental Indenture.

This Supplemental Indenture No. 1 is executed and shall be construed as an indenture supplemental to the Indenture and, as provided in the Indenture, this Supplemental Indenture No. 1 forms a part thereof.


(c) Disclosure.

Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Capital Corporation (assignee of Emerson Finance Co.), a Delaware corporation. The address of the beneficiary is 8000 West Florissant Avenue, St. Louis, Missouri 63136, Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at

100 Federal Street, Boston, Massachusetts 02110, Attention of
Corporate Trust Division.

IN WITNESS WHEREOF, the Owner Trustee and the Indenture Trustee have each caused this Supplemental Indenture No. 1 to be duly executed by their respective officers thereunto duly authorized, all as of the date first set forth above.

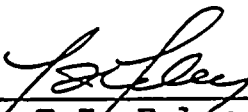
THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under the Trust
Agreement dated as of August 1,
1986, with Emerson Capital
Corporation (assignee of
Emerson Finance Co.)

By 

Martin P. Henry
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK,
as Indenture Trustee

By 

T.J. Foley
Vice President

Date: November 19, 1986

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 19th day of November, 1986, before me personally came MARTIN P. HENRY, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Boston, Massachusetts; that he is Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, described in and which executed the foregoing instrument; and that he signed his name thereto on behalf of said association by authority of the Board of Directors of said corporation.

David A. Spaw

Notary Public

[NOTARIAL SEAL]

Term Expires:

Commission Expires March 30, 1987

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

On the 19th day of November, 1986, before me personally came T.J. FOLEY, to me known, who, being by me duly sworn, did acknowledge, depose and say that he resides at Bethpage, New York; that he is a Vice President of CHEMICAL BANK, a New York banking corporation described in and which executed the foregoing instrument; and that he signed his name thereto on behalf of said corporation by authority of the Board of Directors of said corporation.

David A. Spork

Notary Public

[NOTARIAL SEAL]

Term Expires:

17

EXHIBIT A-1
TO SUPPLEMENT NO. 1

FORM OF REFUNDING NOTE
(DUE DECEMBER 30, 1998)

THIS NOTE HAS NOT BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933 AND MAY NOT BE TRANSFERRED,
SOLD OR OFFERED FOR SALE IN VIOLATION OF SUCH ACT

NONRECOURSE PROMISSORY NOTE, REFUNDING SERIES 1986
(DUE DECEMBER 30, 1998)

Issued at: New York, New York

Issue Date: November 19, 1986

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (Owner Trustee) under a Trust Agreement dated as of August 1, 1986 with Emerson Capital Corporation (assignee of Emerson Finance Co.) (the Equity Participant), hereby promises to pay to PVNGS FUNDING CORP., INC., or registered assigns, the principal sum of Twenty Million Nine Hundred Fifty Six Thousand Dollars (\$20,956,000), such payment to be made in the amounts and on the dates specified in Schedule 1 hereto, as such Schedule 1 may be revised in accordance herewith; and to pay interest (computed on the basis of a 360-day year of twelve 30-day months) on the aggregate amount of such principal sum remaining unpaid from time to time from the date of this Refunding Note until due and payable, semiannually in arrears on June 30 and December 30 in each year, commencing December 30, 1986, at the rate of 9.00% per annum, until the principal hereof is paid in full.

Capitalized terms used in this Refunding Note which are not otherwise defined herein shall have the meanings ascribed thereto in the Indenture (as hereinafter defined).

In the event any date on which a payment is due under this Refunding Note is not a Business Day, then payment thereof may be made on the next succeeding Business Day with the same force and effect as if made on the date on which such payment was due and no

interest in respect of such payment shall accrue for the period from and after such date.

All payments of principal, and premium, if any, and interest to be made by the Owner Trustee hereunder and under the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986, as at any time heretofore or hereafter amended or supplemented in accordance with the provisions thereof (the Indenture), between the Owner Trustee and Chemical Bank, as Trustee (the Indenture Trustee), shall be made only from the Lease Indenture Estate and the Trust Estate and the Indenture Trustee shall have no obligation for the payment thereof except to the extent that the Indenture Trustee shall have sufficient income or proceeds from the Lease Indenture Estate to make such payments in accordance with the terms of Article V of the Indenture. The Holder hereof, by its acceptance of this Refunding Note, agrees that such Holder will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to the Holder hereof as above provided, and that neither the Equity Participant nor, except as expressly provided in the Indenture, the Owner Trustee nor the Indenture Trustee is or shall be personally liable to the Holder hereof for any amounts payable under this Refunding Note or for any performance to be rendered under the Indenture or any other Transaction Document or for any liability thereunder; provided, however, that in the event the Lessee shall assume all the obligations of the Owner Trustee hereunder and under the Indenture pursuant to Section 3.9(b) of the Indenture, then all the payments to be made under this Refunding Note shall be made only from payments made by the Lessee under this Refunding Note in accordance with the Assumption Agreement referred to in said Section 3.9(b) and the Holder of this Refunding Note agrees that in such event it will look solely to the Lessee for such payment and, subject to Section 2.4 of the Indenture, to the Lease Indenture Estate.

Principal, and premium, if any, and interest shall be payable in immediately available funds 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, in the manner provided in the Indenture, on presentment of this Refunding Note at the Indenture Trustee's Office, or as otherwise provided in the Indenture.

In the manner and to the extent provided in the Indenture, Schedule 1 hereto may be adjusted once at the discretion of the Owner

Trustee prior to June 30, 1989, in connection with an adjustment to Basic Rent under Section 3(d) of the Facility Lease.

In the event of any partial prepayment of this Refunding Note (other than pursuant to the payment of principal in accordance with Schedule 1 hereto), the principal amount of this Refunding Note to be paid thereafter pursuant to Schedule 1 hereto shall be adjusted proportionately; provided that, all such adjustments shall be rounded to the nearest \$1000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of this Refunding Note which is prepaid. In connection with such adjustments the Owner Trustee shall deliver to the Indenture Trustee, not later than 60 days prior to the next date on which a payment of principal of this Refunding Note is due following such partial prepayment, a revised Schedule 1 hereto. The Indenture Trustee may rely on such revised Schedule 1 and shall have no duty with respect to the adjustments set forth therein other than to make it available for inspection by the Holder of this Note.

The Holder hereof, by its acceptance of this Refunding Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. The Holder of this Refunding Note agrees, by its acceptance hereof, that it will duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Refunding Note unless and until all such notations have been duly made.

This Refunding Note is one of the Refunding Notes referred to in the Indenture. The Indenture permits the issuance of additional series of Notes, as provided in Section 3.5 of the Indenture, and the several series may be for varying aggregate principal amounts and may have different maturity dates, interest rates, redemption provisions and other terms. The properties of the Owner Trustee included in the Lease Indenture Estate are pledged to the Indenture Trustee to the extent provided in the Indenture as security for the payment of the principal of and premium, if any, and interest on this Refunding Note and all other Notes issued and outstanding from time to time under the Indenture. Reference is hereby made to the Indenture for a statement of the rights of the Holders of, and the nature and extent of the security for, this Refunding Note and of the rights of, and the nature and extent of the security for, the Holders of the other Notes and of certain rights of the Owner Trustee, as well as for a statement of the terms and conditions of the trust

created by the Indenture, to all of which terms and conditions the Holder hereof agrees by its acceptance of this Refunding Note.

This Refunding Note is subject to purchase by the Owner Trustee as provided in Section 6.8(b) of the Indenture and to mandatory prepayment in full as provided in Section 5.2 of the Indenture, such prepayment being without premium but including accrued interest to the date of prepayment. In addition, this Refunding Note may be prepaid in whole or in part at any time on or after December 30, 1991 by the Owner Trustee as follows: upon the giving of not less than 30 days' notice as provided in the Indenture and at the following prepayment prices (expressed as a percentage of the unpaid principal amount hereof), together with interest accrued to the date fixed for prepayment:

<u>If prepaid during the twelve months beginning December 30,</u>	<u>Prepayment Price</u>
1991	104.50%
1992	103.60%
1993	102.70%
1994	101.80%
1995	100.90%

and thereafter at the principal amount thereof, together with interest accrued to the date fixed for prepayment.

In case an Indenture Event of Default shall occur and be continuing, the unpaid balance of the principal of this Refunding Note and any other Notes, together with all accrued but unpaid interest thereon, may, subject to certain rights of the Owner Trustee and the Equity Participant contained or referred to in the Indenture, be declared or may become due and payable in the manner and with the effect provided in the Indenture.

The lien upon the Lease Indenture Estate is subject to being legally discharged prior to the maturity of this Refunding Note upon the deposit with the Indenture Trustee of cash or certain securities sufficient to pay this Refunding Note when due in accordance with the terms of the Indenture.

There shall be maintained at the Indenture Trustee's Office a register for the purpose of registering transfers and exchanges of Notes in the manner provided in the Indenture. The transfer of this Refunding Note is registrable, as provided in the Indenture, upon surrender of this Refunding Note for registration of transfer duly accompanied by a written instrument of transfer duly executed by or on behalf of the registered Holder hereof, together with the amount of any applicable transfer taxes. Prior to due presentment for registration of transfer of this Refunding Note, the Owner Trustee and the Indenture Trustee may treat the person in whose name this Refunding Note is registered as the owner hereof for the purpose of receiving payments of principal of and premium, if any, and interest on this Refunding Note and for all other purposes whatsoever, whether or not this Refunding Note be overdue, and neither the Owner Trustee nor the Indenture Trustee shall be affected by notice to the contrary.

This Refunding Note shall be governed by, and construed in accordance with, the law of the State of New York.

IN WITNESS WHEREOF, the Owner Trustee has caused this Refunding Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under a Trust Agreement
dated as of August 1, 1986 with
Emerson Capital Corporation
(assignee of Emerson Finance
Co.)

By _____
Martin P. Henry
Assistant Vice President

This Note is one of the series of Notes referred to therein
and in the within-mentioned Indenture.

CHEMICAL BANK,
as Indenture Trustee

By _____
T.J. Foley
Vice President

SCHEDULE 1
TO THE REFUNDING NOTE
(DUE DECEMBER 30, 1998)

Schedule of Principal Amortization

<u>Payment Date</u>	<u>Principal Amount Payable</u>	<u>Principal Balance</u>
June 30, 1990	\$ 128,000	\$20,828,000
December 30, 1990	594,000	20,234,000
June 30, 1991	621,000	19,613,000
December 30, 1991	649,000	18,964,000
June 30, 1992	678,000	18,286,000
December 30, 1992	708,000	17,578,000
June 30, 1993	740,000	16,838,000
December 30, 1993	773,000	16,065,000
June 30, 1994	808,000	15,257,000
December 30, 1994	845,000	14,412,000
June 30, 1995	883,000	13,529,000
December 30, 1995	922,000	12,607,000
June 30, 1996	964,000	11,643,000
December 30, 1996	1,007,000	10,636,000
June 30, 1997	1,053,000	9,583,000
December 30, 1997	3,055,000	6,528,000
June 30, 1998	3,192,000	3,336,000
December 30, 1998	3,336,000	0

Principal Amount	<u><u>\$20,956,000</u></u>
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ASSIGNMENT

Date: November 19, 1986

For value received, PVNGS FUNDING CORP., INC. hereby sells, assigns and transfers to CHEMICAL BANK as Collateral Trust Trustee pursuant to the Collateral Trust Indenture dated as of November 1, 1986, as heretofore amended and supplemented, among PVNGS FUNDING CORP., INC., Arizona Public Service Company and said Collateral Trust Trustee, without recourse, the Refunding Note to which this Assignment is annexed and all rights thereunder.

PVNGS FUNDING CORP., INC.

By _____
Vice President

EXHIBIT A-2
TO SUPPLEMENT NO. 1

FORM OF REFUNDING NOTE
(DUE JUNE 30, 2015)

THIS NOTE HAS NOT BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933 AND MAY NOT BE TRANSFERRED,
SOLD OR OFFERED FOR SALE IN VIOLATION OF SUCH ACT

NONRECOURSE PROMISSORY NOTE, REFUNDING SERIES 1986
(DUE JUNE 30, 2015)

Issued at: New York, New York

Issue Date: November 19, 1986

FOR VALUE RECEIVED, THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (Owner Trustee) under a Trust Agreement dated as of August 1, 1986 with Emerson Capital Corporation (assignee of Emerson Finance Co.) (the Equity Participant), hereby promises to pay to PVNGS FUNDING CORP., INC., or registered assigns, the principal sum of One Hundred Thirty Nine Million Forty Four Thousand Dollars (\$139,044,000), such payment to be made in the amounts and on the dates specified in Schedule 1 hereto, as such Schedule 1 may be revised in accordance herewith; and to pay interest (computed on the basis of a 360-day year of twelve 30-day months) on the aggregate amount of such principal sum remaining unpaid from time to time from the date of this Refunding Note until due and payable, semiannually in arrears on June 30 and December 30 in each year, commencing December 30, 1986, at the rate of 10.45% per annum, until the principal hereof is paid in full.

Capitalized terms used in this Refunding Note which are not otherwise defined herein shall have the meanings ascribed thereto in the Indenture (as hereinafter defined).

In the event any date on which a payment is due under this Refunding Note is not a Business Day, then payment thereof may be made on the next succeeding Business Day with the same force and effect as if made on the date on which such payment was due and no interest in respect of such payment shall accrue for the period from and after such due date.

All payments of principal, and premium, if any, and interest to be made by the Owner Trustee hereunder and under the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease dated as of August 1, 1986, as at any time heretofore or hereafter amended or supplemented in accordance with the provisions thereof (the Indenture), between the Owner Trustee and Chemical Bank, as Trustee (the Indenture Trustee), shall be made only from the Lease Indenture Estate and the Trust Estate and the Indenture Trustee shall have no obligation for the payment thereof except to the extent that the Indenture Trustee shall have sufficient income or proceeds from the Lease Indenture Estate to make such payments in accordance with the terms of Article V of the Indenture. The Holder hereof, by its acceptance of this Refunding Note, agrees that such Holder will look solely to the Trust Estate and the income and proceeds from the Lease Indenture Estate to the extent available for distribution to the Holder hereof as above provided, and that neither the Equity Participant nor, except as expressly provided in the Indenture, the Owner Trustee nor the Indenture Trustee is or shall be personally liable to the Holder hereof for any amounts payable under this Refunding Note or for any performance to be rendered under the Indenture or any other Transaction Document or for any liability thereunder; provided, however, that in the event the Lessee shall assume all the obligations of the Owner Trustee hereunder and under the Indenture pursuant to Section 3.9(b) of the Indenture, then all the payments to be made under this Refunding Note shall be made only from payments made by the Lessee under this Refunding Note in accordance with the Assumption Agreement referred to in said Section 3.9(b) and the Holder of this Refunding Note agrees that in such event it will look solely to the Lessee for such payment and, subject to Section 2.4 of the Indenture, to the Lease Indenture Estate.

Principal, and premium, if any, and interest shall be payable in immediately available funds 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, in the manner provided in the Indenture, on presentment of this Refunding Note at the Indenture Trustee's Office, or as otherwise provided in the Indenture.

In the manner and to the extent provided in the Indenture, Schedule 1 hereto may be adjusted once at the discretion of the Owner Trustee prior to June 30, 1989, in connection with an adjustment to Basic Rent under Section 3(d) of the Facility Lease.

In the event of any partial prepayment of this Refunding Note (other than pursuant to the payment of principal in accordance with Schedule 1 hereto), the principal amount of this Refunding Note to be paid thereafter pursuant to Schedule 1 hereto shall be adjusted proportionately; provided that; all such adjustments shall be rounded to the nearest \$1000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of this Refunding Note which is prepaid. In connection with such adjustments the Owner Trustee shall deliver to the Indenture Trustee, not later than 60 days prior to the next date on which a payment of principal of this Refunding Note is due following such partial prepayment, a revised Schedule 1 hereto. The Indenture Trustee may rely on such revised Schedule 1 and shall have no duty with respect to the adjustments set forth therein other than to make it available for inspection by the Holder of this Note.

The Holder hereof, by its acceptance of this Refunding Note, agrees that each payment received by it hereunder shall be applied in the manner set forth in Section 3.11 of the Indenture. The Holder of this Refunding Note agrees, by its acceptance hereof, that it will duly note by appropriate means all payments of principal or interest made hereon and that it will not in any event transfer or otherwise dispose of this Refunding Note unless and until all such notations have been duly made.

This Refunding Note is one of the Refunding Notes referred to in the Indenture. The Indenture permits the issuance of additional series of Notes, as provided in Section 3.5 of the Indenture, and the several series may be for varying aggregate principal amounts and may have different maturity dates, interest rates, redemption provisions and other terms. The properties of the Owner Trustee included in the Lease Indenture Estate are pledged to the Indenture Trustee to the extent provided in the Indenture as security for the payment of the principal of and premium, if any, and interest on this Refunding Note and all other Notes issued and outstanding from time to time under the Indenture. Reference is hereby made to the Indenture for a statement of the rights of the Holders of, and the nature and extent of the security for, this Refunding Note and of the rights of, and the nature and extent of the security for, the Holders of the other Notes and of certain rights of the Owner Trustee, as well as for a statement of the terms and conditions of the trust created by the Indenture, to all of which terms and conditions the Holder hereof agrees by its acceptance of this Refunding Note.

This Refunding Note is subject to purchase by the Owner Trustee as provided in Section 6.8(b) of the Indenture and to mandatory prepayment in full as provided in Section 5.2 of the Indenture, such prepayment being without premium but including accrued interest to the date of prepayment. In addition, this Refunding Note may be prepaid in whole or in part at any time on or after December 30, 1991 by the Owner Trustee as follows: upon the giving of not less than 30 days' notice as provided in the Indenture and at the following prepayment prices (expressed as a percentage of the unpaid principal amount hereof), together with interest accrued to the date fixed for prepayment:

<u>If prepaid during the twelve months beginning December 30,</u>	<u>Prepayment Price</u>
1991	107.70%
1992	107.15%
1993	106.60%
1994	106.05%
1995	105.50%
1996	104.95%
1997	104.40%
1998	103.85%
1999	103.30%
2000	102.75%
2001	102.20%
2002	101.65%
2003	101.10%
2004	100.55%

and thereafter at the principal amount thereof, together with interest accrued to the date fixed for prepayment.

In case an Indenture Event of Default shall occur and be continuing, the unpaid balance of the principal of this Refunding Note and any other Notes, together with all accrued but unpaid interest thereon, may, subject to certain rights of the Owner Trustee and the Equity Participant contained or referred to in the Indenture, be

declared or may become due and payable in the manner and with the effect provided in the Indenture.

The lien upon the Lease Indenture Estate is subject to being legally discharged prior to the maturity of this Refunding Note upon the deposit with the Indenture Trustee of cash or certain securities sufficient to pay this Refunding Note when due in accordance with the terms of the Indenture.

There shall be maintained at the Indenture Trustee's Office a register for the purpose of registering transfers and exchanges of Notes in the manner provided in the Indenture. The transfer of this Refunding Note is registrable, as provided in the Indenture, upon surrender of this Refunding Note for registration of transfer duly accompanied by a written instrument of transfer duly executed by or on behalf of the registered Holder hereof, together with the amount of any applicable transfer taxes. Prior to due presentment for registration of transfer of this Refunding Note, the Owner Trustee and the Indenture Trustee may treat the person in whose name this Refunding Note is registered as the owner hereof for the purpose of receiving payments of principal of and premium, if any, and interest on this Refunding Note and for all other purposes whatsoever, whether or not this Refunding Note be overdue, and neither the Owner Trustee nor the Indenture Trustee shall be affected by notice to the contrary.

This Refunding Note shall be governed by, and construed in accordance with, the law of the State of New York.

IN WITNESS WHEREOF, the Owner Trustee has caused this Refunding Note to be duly executed as of the date hereof.

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual
capacity, but solely as Owner
Trustee under a Trust Agreement
dated as of August 1, 1986 with
Emerson Capital Corporation
(assignee of Emerson Finance
Co.)

By _____
Martin P. Henry
Assistant Vice President

This Note is one of the series of Notes referred to therein
and in the within-mentioned Indenture.

CHEMICAL BANK,
as Indenture Trustee

By _____
T.J. Foley
Vice President

SCHEDULE 1
TO THE REFUNDING NOTE
(DUE JUNE 30, 2015)

Schedule of Principal Amortization

<u>Payment Date</u>	<u>Principal Amount Payable</u>	<u>Principal Balance</u>
June 30, 1999	\$1,110,000	\$137,934,000
December 30, 1999	2,223,000	135,711,000
June 30, 2000	2,539,000	133,172,000
December 30, 2000	2,381,000	130,791,000
June 30, 2001	2,716,000	128,075,000
December 30, 2001	2,547,000	125,528,000
June 30, 2002	2,906,000	122,622,000
December 30, 2002	2,724,000	119,898,000
June 30, 2003	3,108,000	116,790,000
December 30, 2003	2,913,000	113,877,000
June 30, 2004	3,325,000	110,552,000
December 30, 2004	3,115,000	107,437,000
June 30, 2005	3,556,000	103,881,000
December 30, 2005	3,332,000	100,549,000
June 30, 2006	3,804,000	96,745,000
December 30, 2006	3,564,000	93,181,000
June 30, 2007	4,069,000	89,112,000
December 30, 2007	3,811,000	85,301,000
June 30, 2008	4,352,000	80,949,000
December 30, 2008	4,076,000	76,873,000
June 30, 2009	4,655,000	72,218,000
December 30, 2009	4,360,000	67,858,000
June 30, 2010	4,979,000	62,879,000
December 30, 2010	4,663,000	58,216,000
June 30, 2011	5,326,000	52,890,000
December 30, 2011	4,987,000	47,903,000
June 30, 2012	5,697,000	42,206,000
December 30, 2012	6,632,000	35,574,000
June 30, 2013	4,751,000	30,823,000
December 30, 2013	7,088,000	23,735,000
June 30, 2014	7,540,000	16,195,000

<u>Payment Date</u>	<u>Principal Amount Payable</u>	<u>Principal Balance</u>
December 30, 2014	9,905,000	6,290,000
June 30, 2015	6,290,000	0

Principal Amount	<u><u>\$139,044,000</u></u>
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ASSIGNMENT

Date: November 19, 1986

For value received, PVNGS FUNDING CORP., INC. hereby sells, assigns and transfers to CHEMICAL BANK as Collateral Trust Trustee pursuant to the Collateral Trust Indenture dated as of November 1, 1986, as heretofore amended and supplemented, among PVNGS FUNDING CORP., INC., Arizona Public Service Company and said Collateral Trust Trustee, without recourse, the Refunding Note to which this Assignment is annexed and all rights thereunder.

PVNGS FUNDING CORP., INC.

By _____
Vice President

ASSIGNMENT, ASSUMPTION

AND

FURTHER AGREEMENT

dated as of August 1, 1986

between

ARIZONA PUBLIC SERVICE COMPANY,

and

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity, but
solely as Owner Trustee under a Trust
Agreement with Emerson Finance Co.

Sale and Leaseback of an Undivided Interest
in Palo Verde Nuclear Generating Station Unit 2

THIS ASSIGNMENT, ASSUMPTION AND FURTHER AGREEMENT, dated as of August 1, 1986, between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), and THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (the Owner Trustee), under a Trust Agreement, dated as of August 1, 1986, with EMERSON FINANCE CO., a Delaware corporation, as Equity Participant (the Equity Participant).

W I T N E S S E T H :

WHEREAS, APS and the other ANPP Participants are parties to the ANPP Participation Agreement (such terms and all other terms used in these recitals without definition having the respective definitions to which reference is made in Article I below); and

WHEREAS, APS has sold, and the Owner Trustee has purchased, the Undivided Interest and the Real Property Interest for and in consideration of the payment to APS by the Owner Trustee of the Purchase Price, the purchase price of the Real Property Interest and the assignments and assumptions herein set forth;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

For purposes hereof, unless otherwise defined herein, capitalized terms used herein shall have the meanings assigned to such terms in Appendix A hereto. References in this Agreement to articles, sections and clauses are to articles, sections and clause in this Agreement unless otherwise indicated.

ARTICLE II

NONPARTITIONMENT

SECTION 2.01. Nonpartitionment. The Owner Trustee hereby waives any rights it may have to partition Unit 2, whether by partitionment in kind or by sale and division of proceeds, and further agrees that it will not resort to any action in law or in equity to partition Unit 2, and it waives the benefits of all laws that may now or hereafter authorize such partition for a term (i) which shall be coterminous with the ANPP Participation Agreement or (ii) which shall be for such lesser period as may be required under Applicable Law.

ARTICLE III

ASSIGNMENTS; EXERCISE OF RIGHTS

SECTION 3.01. Assignment of Warranties. The Lessee hereby ASSIGNS to the Owner Trustee an undivided interest, equal to the Unit 2 Interest in, to and under all of APS's rights under any and all warranties of and other claims against dealers, manufacturers, vendors, contractors and subcontractors relating to Unit 2.

SECTION 3.02. Assignment of the ANPP Participation Agreement. (a) The Lessee hereby ASSIGNS to the Owner Trustee an undivided interest, equal to the Unit 2 Interest in, to and under all of APS's rights under the ANPP Participation Agreement, to the extent that such rights relate to the Undivided Interest (including, but without limitation, a percentage entitlement equal to the Unit 2 Interest of the Net Energy Generation and Available Generating Capability (as each such term is defined in the ANPP Participation Agreement) of Unit 2).

(b) The Owner Trustee hereby ASSIGNS to the Lessee the rights assigned under paragraph (a) until the Lease Termination Date.

SECTION 3.03. Exercise of Rights as Participant under the ANPP Participation Agreement. (a) Except as provided in Sections 15.2.2, 15.6.4 and 15.10 of the ANPP Participation Agreement (or any comparable successor provision) APS shall be and remain the sole "Participant" for all purposes of the ANPP

Participation Agreement and the sole representative (with power to bind) in all dealings with the other ANPP Participants in relation to the Undivided Interest, the Real Property Interest and the rights assigned to the Owner Trustee pursuant to this Agreement; provided, however, that the foregoing shall not limit in any way any liability or obligation that APS may incur to the Owner Trustee or the Equity Participant under any Transaction Document as a result thereof.

(b) Unless the ANPP Participation Agreement shall otherwise permit, any right conferred on the Owner Trustee by Section 15.2.2 of the ANPP Participation Agreement shall be exercised as required by Section 15.6.3.3 of said Agreement.

(c) The provisions of this Section 3.03 shall remain in full force and effect until such time as the ANPP Administrative Committee or the ANPP Participants shall otherwise consent by amendment to the ANPP Participation Agreement or otherwise.

ARTICLE IV

ASSUMPTION; RELEASE

SECTION 4.01. Assumption by Owner Trustee. Except as contemplated by Section 5(a) of the Facility Lease, the Owner Trustee agrees that, effective on and as of the Lease Termination Date (unless a Transferee (Transferee) shall have qualified under Section 15.10 of the ANPP Participation Agreement or any comparable successor provision), unless a Default or Event of Default shall have occurred and be continuing or an Event of Loss shall have occurred or a Deemed Loss Event shall have been declared, the Owner Trustee shall assume and agree to pay, perform and discharge the Unit 2 Interest of all liabilities and obligations of APS under, or with respect to, the ANPP Project Agreements, attributable to Unit 2, other than any and all costs relating to, allocable to, or incurred in connection with, Decommissioning.

SECTION 4.02. Release. Upon the assumption and agreement by a Transferee pursuant to Section 4.01 (whether at the Lease Termination Date or thereafter), the Owner Trustee shall therewith and thereupon be released and discharged from its obligations under

Section 4.01 arising on or after such assumption and agreement.

ARTICLE V

NO RELEASE OF APS; REIMBURSEMENT

SECTION 5.01. No Release of APS. Notwithstanding the provisions of Article IV or any other provision hereof or of any other Transaction Document, and except to the extent provided in Section 15.10 of the ANPP Participation Agreement (or any comparable successor provision), APS shall not be released from any liability or obligation under the ANPP Project Agreements, or otherwise, with respect to PVNGS, and APS shall remain liable for the payment and performance of all such liabilities and obligations, including, without limitation, any and all liabilities and obligations not assumed by the Owner Trustee or a Transferee pursuant to Section 4.01.

SECTION 5.02. Reimbursement. Unless a Default or an Event of Default shall have occurred and be continuing or an Event of Loss shall have occurred or a Deemed Loss Event shall have been declared, from and after the Lease Termination Date, upon the payment or performance by APS of any liability or obligation in respect of which the Owner Trustee shall also have become obligated in consequence of Article IV, and for so long as the Owner Trustee shall be so liable, APS shall be entitled to prompt reimbursement by the Owner Trustee for all amounts expended in connection with such payment or performance.

ARTICLE VI

FURTHER AGREEMENTS OF APS

SECTION 6.01. Agreement to Sell or Lease Unit 2 Retained Assets. Upon a transfer to a Transferee, APS agrees in respect of the Undivided Interest and the Real Property Interest, (i) if such Transferee is a purchaser of the Undivided Interest and the Real Property Interest, to sell to such Transferee, at a price equal to the Unit 2 Retained Assets Portion of the combined proceeds of the sale of the Undivided Interest and the undivided interest in the Unit 2

Retained Assets, an undivided interest, equal to the Unit 2 Interest, in and to the Unit 2 Retained Assets, or (ii) if the Transferee is a lessee of the Undivided Interest and the Real Property Interest, to lease to the Owner Trustee, at a rent equal to the Unit 2 Retained Assets Portion of the total rent received by the Owner Trustee from such Transferee, an undivided interest, equal to the Unit 2 Interest, in and to the Unit 2 Retained Assets, whereupon the Owner Trustee shall sub-lease or otherwise make available to such Transferee such undivided interest in and to such Unit 2 Retained Assets. Any such sale or lease by APS shall be accomplished by an appropriate bill of sale or lease.

SECTION 6.02. Agreement to Assign or Make Available ANPP Project Agreements. Upon a transfer to a Transferee, APS agrees in respect of the Undivided Interest and the Real Property Interest, (i) if the Transferee is a purchaser of the Undivided Interest and the Real Property Interest, to assign to such Transferee an undivided interest, equal to the Unit 2 Interest, in the ANPP Project Agreements (other than the ANPP Participation Agreement) to the extent relating to Unit 2 and the Unit 2 Retained Assets, and (ii) if such Transferee is a lessee of the Undivided Interest and the Real Property Interest, to assign for the term of such lease to such Transferee an undivided interest, equal to the Unit 2 Interest, in the ANPP Project Agreements (other than the ANPP Participation Agreement) to the extent relating to Unit 2 and the Unit 2 Retained Assets. Any assignment pursuant to this Section 6.02 shall be accomplished by an appropriate instrument of assignment.

SECTION 6.03. Agreements to Seek Amendments to the ANPP Participation Agreement and the License. The Lessee agrees to use its best efforts to obtain any required amendments to the ANPP Participation Agreement and the License to permit APS to act as Agent of the Owner Trustee in the manner contemplated by Section 7.01 hereof, if (i) APS shall not have elected to purchase the Undivided Interest as provided in Section 13(b) of the Facility Lease and (ii) there shall not be a Transferee in respect of the Undivided Interest and the Real Property Interest.

ARTICLE VII

INTERIM AGENCY ARRANGEMENTS

SECTION 7.01. Designation of Agent. From and after the Lease Termination Date (or during such period on or after the Lease Termination Date that the Owner Trustee shall have waived any Default or Event of Default with respect to the inability of the Lessee to surrender possession as required by Section 5(a) of the Facility Lease and until a transfer to a Transferee in respect of the Undivided Interest and the Real Property Interest (such period being referred to as the Agency Period), APS shall be, and the Owner Trustee hereby designates APS as, the initial agent (the Agent) of the Owner Trustee in the exercise of all rights assigned to the Owner Trustee hereunder. The Owner Trustee may terminate such agreement and the Agency Period at any time.

SECTION 7.02. Operation of Unit 2. During the Agency Period, the Agent shall administer the operation of the Undivided Interest and the Real Property Interest in accordance with this Agreement and all instructions of the Owner Trustee in accordance with Applicable Law. If, however, the Owner Trustee shall, prior to, or at any time during, the Agency Period, enter into any joint ownership and operating agreement with other Persons having a legal right to, or right to use, any other undivided interest in Unit 2, the Agent agrees to join in, and be bound by, the terms of such agreement if the Agent's performance thereunder shall not violate, or result in a violation of, any Applicable Law or the License. The Owner Trustee agrees to give the Agent reasonable prior written notice of the commencement of the negotiation of any such agreement.

SECTION 7.03. ANPP Participation Agreement. The Lessee agrees that, at all times during the Agency Period, it will perform all obligations and discharge all liability for which it is responsible as a "Participant" under the ANPP Participation Agreement in respect of the Undivided Interest and the Real Property Interest. In the performance of the foregoing agreement, APS shall have no obligation to exercise its rights as an ANPP Participant to cause Capital Improvements to be made to Unit 2 unless the Owner Trustee shall have agreed to provide funds for the payment of the Lessor's Portion of the cost of such

Capital Improvements to APS prior to the date on which such amounts shall be due with respect thereto under the ANPP Participation Agreement.

SECTION 7.04. Support. Except with respect to the Unit 2 Retained Assets for which provision is made in Section 7.06, APS covenants and agrees that, at all times during the Agency Period, it will provide, or make available, to the Owner Trustee such rights of the Lessee in and to other assets owned by APS and the ANPP Project Agreements, to the extent relating to the Undivided Interest and the Real Property Interest, as are necessary for the performance of the obligations of the Lessee hereunder.

SECTION 7.05. Compensation. As compensation for its obligations under Sections 7.02, 7.03 and 7.04, APS shall be entitled to receive, and the Owner Trustee hereby agrees to pay, an amount equal to (i) the Lessor's Portion of the aggregate of (A) amounts paid by APS as provided in Section 7.03 to the extent reasonably allocable to Unit 2 and (B) out-of-pocket expenses incurred by APS or the Agent, as the case may be, in connection with the performance of its agreements in this Article VII and (ii) the Unit 2 Retained Assets Portion of the net proceeds of the sale of power and energy in respect of Lessor's Portion of the Generation Entitlement Share. Compensation under (A) clause (i) of this Section 7.05 (which shall not exceed the fair market value for the obligations performed) shall be paid promptly in cash upon receipt of an invoice from APS and (B) clause (ii) of this Section 7.05 shall be paid promptly after receipt by the Owner Trustee.

SECTION 7.06. Transmission; Transmission Agreement. (a) The Lessee covenants and agrees that, at all times during the Agency Period, the Owner Trustee shall have the right to wheel, under normal transmission operating conditions, power and energy to which the Owner Trustee is entitled hereunder and under the other Transaction Documents and under the ANPP Participation Agreement, under normal transmission operating conditions, over transmission equipment in which APS now owns or may hereafter acquire an ownership interest, between Unit 2 and the ANPP Switchyard on terms and conditions no less favorable than those being offered to other similarly situated Persons.

(b) Based upon the respective rights, duties and obligations of the Owner Trustee and APS set forth in Section 7.06(a), if APS shall fail or decline to give the notice of renewal of the Facility Lease or purchase of the Undivided Interest, in each case as provided in Section 13(a) of the Facility Lease, APS and the Owner Trustee shall forthwith commence the negotiation in good faith of a definitive transmission agreement, not inconsistent with the terms and provisions of Section 7.06(a), but containing sufficient detail for the proper wheeling of power and energy, under normal transmission operating conditions, over the equipment of APS referred to in such Section 7.06(a) under then existing circumstances, for the exercise or stipulation, as the case may be, of the respective rights, duties and obligations of the Owner Trustee and APS set forth in Section 7.06(a). The Lessee and the Owner Trustee shall complete such negotiations and execute such definitive transmission agreement prior to the Lease Termination Date and such definitive transmission agreement shall provide for compensation to APS for the transmission services so provided at the Fair Market Sales Value thereof which, for purposes hereof, shall be determined with reference to the compensation then being paid by other similarly situated Persons for which the Lessee is providing such services.

ARTICLE VIII

MISCELLANEOUS

SECTION 8.01. Successors and Assigns. This Agreement shall be binding upon the successors and assigns of each of APS and the Owner Trustee.

SECTION 8.02. Governing Law. The interpretation of this Agreement and the rights and obligations of the parties hereto shall be governed by and construed and enforced in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

SECTION 8.03. Counterpart Execution. This Agreement may be executed in any number of counterparts and by each of the parties hereto on separate counterparts, all such counterparts together constituting but one and the same instrument.

SECTION 8.04. Amendments. The terms of this Agreement shall not be waived, altered, modified, amended, supplemented or terminated in any manner whatsoever, except by written instrument signed by APS and the Owner Trustee.

SECTION 8.05. Survival. All agreements and covenants contained in this Agreement or any agreement, document or certificate delivered pursuant hereto or in connection herewith shall survive the execution and delivery of this Agreement.

SECTION 8.06. Severability of Provisions. Any provision of this Agreement which may be determined by competent authority to be prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and no such prohibition or unenforceability in any jurisdiction shall invalidate or render unenforceable such provisions in any other jurisdiction. To the extent permitted by Applicable Law, APS hereby waives any provision of law which renders any provision hereof prohibited or unenforceable in any respect.

SECTION 8.07. Headings. The division of this Agreement into sections, the provision of a table of contents and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Agreement.

SECTION 8.08. Disclosure of Beneficiary. Pursuant to Arizona Revised Statutes §33-401, the beneficiary of the Trust Agreement is Emerson Finance Co., a Delaware corporation, whose address is 111 East Prospect, Stamford, CT 06904: Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts, 02110, Attention of Corporate Trust Division.

SECTION 8.09. Capacity of Lessee. Notwithstanding anything to the contrary in this Agreement, both parties hereto agree that all rights and obligations of the Lessee with respect to PVNGS under this Agreement are rights and obligations of the Lessee solely in its capacity as an ANPP Participant and not in its capacity as Operating Agent.

IN WITNESS WHEREOF, the parties hereto have each caused this Agreement to be duly executed in New York, New York by their respective officers thereunto duly authorized.

ARIZONA PUBLIC SERVICE
COMPANY

By


Paul A. Williams II

THE FIRST NATIONAL BANK OF
BOSTON, not in its individual capacity, but solely as Owner Trustee under a Trust Agreement, dated as of August 1, 1986, with Emerson Finance Co.

By:

Assistant Vice President

IN WITNESS WHEREOF, the parties hereto have each caused this Agreement to be duly executed in New York, New York by their respective officers thereunto duly authorized.

ARIZONA PUBLIC SERVICE
COMPANY

By _____
Paul A. Williams II

THE FIRST NATIONAL BANK OF
BOSTON, not in its individ-
ual capacity, but solely as
Owner Trustee under a Trust
Agreement, dated as of
August 1, 1986, with
Emerson Finance Co.

By: 
Assistant Vice President

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

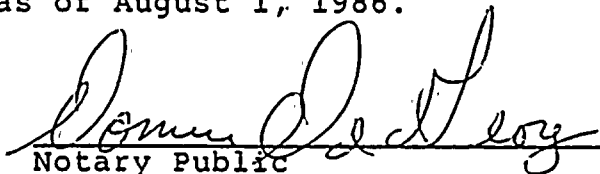
The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Paul A. Williams II, a Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.


Notary Public

DOMINICA DE GEORGE
Notary Public, State of New York
No. 43-4685284
Qualified in Richmond County
Certificate Filed in New York County
Commission Expires January 1, 1989

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Martin P. Henry, an Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association under that certain Trust Agreement dated as of August 1, 1986.


Notary Public

DOMINICA DE GEORGE
Notary Public, State of New York
No. 43-4685284
Qualified in Richmond County
Certificate Filed in New York County
Commission Expires January 1, 1989

When Recorded, Return to: David A. Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

AMENDMENT NO. 1

dated as of November 1, 1986

to

ASSIGNMENT, ASSUMPTION
AND
FURTHER AGREEMENT

dated as of August 1, 1986

between

ARIZONA PUBLIC SERVICE COMPANY

and

THE FIRST NATIONAL BANK OF BOSTON,
not in its individual capacity, but
solely as Owner Trustee under a
Trust Agreement with Emerson Capital Corporation (assignee of
Emerson Finance Co.)

Original Assignment, Assumption and Further Agreement recorded on
August 18, 1986 as Instrument No. 86-439437 in Maricopa County,
Arizona Recorder's Office

AMENDMENT NO. 1, dated as of November 1, 1986, to the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Lessee), and THE FIRST NATIONAL BANK OF BOSTON, not in its individual capacity, but solely as Owner Trustee (the Owner Trustee), under a Trust Agreement, dated as of November 1, 1986, with EMERSON CAPITAL CORPORATION, a Delaware corporation (assignee of Emerson Finance Co.), as Equity Participant (the Equity Participant).

WITNESSETH:

WHEREAS, the Lessee and the Owner Trustee have previously entered into an Assignment, Assumption and Further Agreement, dated as of November 1, 1986 (the Assignment and Assumption Agreement); and

WHEREAS, the Lessee and the Owner Trustee wish to amend the Assignment and Assumption Agreement as herein provided;

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

SECTION 1. Amendments to Assignment and Assumption Agreement.

(a) Sections 3.01, 3.02 and 4.01 of the Assignment and Assumption Agreement are hereby amended by changing the phrase "Unit 2 Interest" to the phrase "Lessor's Portion".

(b) Sections 6.03(i) and 7.06(b) of the Assignment and Assumption Agreement are hereby amended by adding the phrase "and the Real Property Interest" after the phrase "Undivided Interest".

(c) Section 7.01 of the Assignment and Assumption Agreement is hereby amended by changing the phrase "as the Agency Period)" to the phrase "as the Agency Period))".

(d) Section 7.03 of the Assignment and Assumption Agreement is hereby amended by changing the phrase "Lessor's Portion" to the phrase "Unit 2 Interest".

(e) Section 7.05 of the Assignment and Assumption Agreement is hereby amended by changing the first sentence thereof to read in its entirety as follows:

"As compensation for its obligations under Sections 7.02, 7.03 and 7.04, APS shall be entitled to receive, and the Owner

Trustee hereby agrees to pay, in addition to the amounts described in the second sentence of Section 7.03, an amount equal to (i) the Lessor's Portion of out-of-pocket expenses incurred by APS or the Agent, as the case may be, in connection with the performance of its agreements in this Article VII and (ii) the Unit 2 Retained Assets Portion of the net proceeds of the sale of power and energy in respect of the Unit 2 Interest of the Generation Entitlement Share with respect to Unit 2."

(f) Appendix A to the Assignment and Assumption Agreement is hereby deleted and replaced by Appendix A attached hereto.

SECTION 2. Miscellaneous.

(a) Governing Law. The interpretation of this Amendment No. 1 and the rights and obligations of the parties hereto shall be governed by and construed and enforced in accordance with the law of the State of New York, except to the extent that pursuant to the law of the State of Arizona the law of the State of Arizona is mandatorily applicable hereto.

(b) Counterpart Execution. This Amendment No. 1 may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute but one and the same instrument. Although this Amendment No. 1 is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Amendment No. 1 shall be effective on the latest of such dates.

(c) Disclosure. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Capital Corporation (assignee of Emerson Finance Co.), a Delaware corporation. The address of the beneficiary is 8000 West Florissant Avenue, St. Louis, Missouri 63136, Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

IN WITNESS WHEREOF, the parties hereto have each caused this Amendment No. 1 to be duly executed in New York, New York by their respective officers thereunto duly authorized.

ARIZONA PUBLIC SERVICE COMPANY

By: 
Vice President and Treasurer

Date: November 19, 1986

THE FIRST NATIONAL BANK OF
BOSTON, in its individual
capacity and as Owner Trustee

By: 
Assistant Vice President

Date: November 19, 1986

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986 by PAUL A. WILLIAMS II, Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.

David A. Spivak
Notary Public

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4661463
Qualified in New York County
Commission Expires March 30, 1987

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 19th day of November, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under the Trust Agreement dated as of August 1, 1986 with Emerson Capital Corporation (assignee of Emerson Finance Co.).

David A. Spivak
Notary Public

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4661463
Qualified in New York County
Commission Expires March 30, 1987

When recorded, return to:

David Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

DEED AND BILL OF SALE

Dated as of August 18, 1986

between

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona corporation,
as Seller

and

THE FIRST NATIONAL BANK OF BOSTON, a national banking
association, not in its individual capacity, but solely
as Owner Trustee under a Trust Agreement, dated as of
August 1, 1986, with Emerson Finance Co.,
as Buyer

DEED AND BILL OF SALE, dated as of August 18, 1986 between ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the Seller), and THE FIRST NATIONAL BANK OF BOSTON, a national banking association, not in its individual capacity, but solely as Owner Trustee (in such capacity, the Owner Trustee) under the Trust Agreement, dated as of August 1, 1986, with the Equity Participant identified in paragraph 6 hereof (the Owner Trustee in its capacity as owner trustee under the foregoing Trust Agreement being hereinafter referred to as the Buyer).

W I T N E S S E T H :

WHEREAS, the Seller desires to sell, and the Buyer desires to purchase, the Undivided Interest, for and in consideration of the amounts paid by the Buyer to the Seller pursuant to the Participation Agreement (as hereinafter defined);

NOW, THEREFORE, in consideration of the premises and of other good and valuable consideration, receipt of which is hereby acknowledged, the parties hereto agree as follows:

1. For the purpose hereof, capitalized terms used herein, unless otherwise defined herein, shall have the meanings assigned to such terms in Appendix A attached hereto.

The property described in Exhibit B hereto is collectively referred to herein as Unit 2 and the undivided interests therein being conveyed pursuant hereto are referred to collectively herein as the Undivided Interest. Unit 2 is located on the PVNGS Site described in Exhibit A hereto.

2. The Seller does hereby GRANT, BARGAIN, CONVEY, SELL, ASSIGN, TRANSFER AND SET OVER unto the Buyer a 5.2326% undivided interest in Unit 2 TO HAVE AND TO HOLD the same unto the Buyer, its successors and assigns, FOREVER. It is the intent of this Deed and Bill of Sale, that, from and after the date of this Deed and Bill of Sale, Buyer will own a 5.2326% undivided interest in Unit 2, as a tenant in common with the owners of the remaining undivided interests in Unit 2.

3. The Seller does hereby WARRANT AND COVENANT that it is the true and lawful owner of the Undivided Interest and has good right to sell the Undivided Interest, that title to the Undivided Interest is on the date of execution hereof free and clear of all claims, liens, security interests and encumbrances of any nature, other than Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition of such term) and Liens for 1986 taxes not yet due and payable that good, marketable and indefeasible title to the Undivided Interest is hereby conveyed to the Buyer, and that the Seller will forever warrant and defend such title against the claims of all Persons. The foregoing warranties of the Seller are to

the restraint of any other covenant of the Seller otherwise arising by implication by virtue of Arizona Revised Statutes, Section 33-435.

4. The Seller and the Buyer hereby acknowledge and confirm that, as between the Seller and the Buyer, the Undivided Interest is and will remain personal property, and is not, and will not become, an accession to the PVNGS Site or to the Real Property Interest, title thereto being separate and distinct from title to such real property. The Buyer hereby waives any rights it may have to partition Unit 2, including the Undivided Interest, whether by partition in kind or by sale and division of proceeds, and further agrees that it will not resort to any action in law or in equity to partition Unit 2 and it waives the benefits of all laws that may now or hereafter authorize such partition for a term (i) which shall be coterminous with the ANPP Participation Agreement or (ii) which shall be for such lesser period as may be required by Applicable Law.

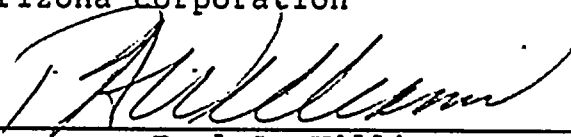
5. Pursuant to the Assignment and Assumption, the Seller has agreed to pay certain costs and expenses relating to Unit 2, including, but without limitation, with respect to decommissioning and retirement of Unit 2, and to perform and comply with certain obligations relating to transfers of interests in Unit 2. All such agreements and obligations of the Seller are hereby incorporated by reference in this Deed and Bill of Sale as if set forth in full herein.

6. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Finance Co., a Delaware corporation (the Equity Participant), whose address is 111 East Prospect, Stamford, CT 06904: Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts, 02110, Attention of Corporate Trust Division.

IN WITNESS WHEREOF, the parties hereto have caused this Deed and Bill of Sale to be executed as of this 18th day of August.

ARIZONA PUBLIC SERVICE COMPANY, an
Arizona corporation

By



Paul A. Williams II

THE FIRST NATIONAL BANK OF BOSTON, a
national banking association, not in
its individual capacity, but solely as
Owner Trustee under the Trust Agreement

By

Assistant Vice President

IN WITNESS WHEREOF, the parties hereto have caused this Deed and Bill of Sale to be executed as of this 18th day of August.

ARIZONA PUBLIC SERVICE COMPANY, an
Arizona corporation

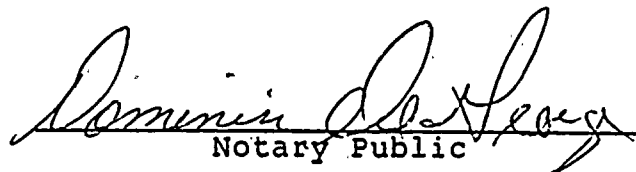
By _____
Paul A. Williams II

THE FIRST NATIONAL BANK OF BOSTON, a
national banking association, not in
its individual capacity, but solely as
Owner Trustee under the Trust Agreement

By _____
Assistant Vice President

State of New York)
) ss:
County of New York)

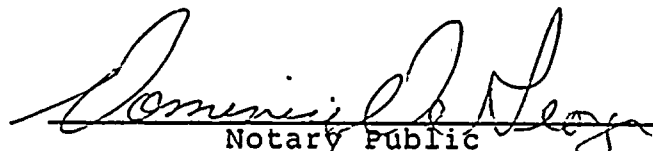
The foregoing instrument was acknowledged before me this 18th day of August, 1986, by PAUL A. WILLIAMS II, the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, on behalf of the corporation.


Notary Public

DOMINICA DE GEORGE
Notary Public, State of New York
No. 43-4685284
Qualified in Richmond County
Certificate Filed in New York County
Commission Expires January 1, 1992

State of New York)
) ss:
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by MARTIN P. HENRY, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as trustee under that certain Trust Agreement dated as of August 1, 1986.


Notary Public

DOMINICA DE GEORGE
Notary Public, State of New York
No. 43-4685284
Qualified in Richmond County
Certificate Filed in New York County
Commission Expires January 1, 1992

EXHIBIT A
to
DEED AND
BILL OF SALE

PVNGS SITE DESCRIPTION

PARCEL NO. 1: Lot Four (4); the Southwest quarter of the Northwest quarter; and the West half of the Southwest quarter, all in Section Two (2), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 2: All of Section Three (3), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 3: The East half of Section Four (4), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 4: The West half of Section Twenty-six (26), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 5: Section Twenty-seven (27), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter of Section 27.

PARCEL NO. 6: The Southeast quarter of Section Twenty-eight (28), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT 50% of all oil, gas and other mineral deposits and geothermal resources recovered from or developed on the property, as reserved in instrument recorded May 10, 1974 in Docket 10647, page 136.

PARCEL NO. 7: The East half of Section Thirty-three (33), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 8: All of Section Thirty-four (34), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 9: The West half of Section Thirty-five (35), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 10: The Southeast quarter of Section Nine (9), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and

Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter thereof.

PARCEL NO. 11: All of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the East half of the Southeast quarter thereof; and EXCEPT the North half of the South half of the Northwest quarter of the Northwest quarter thereof.

PARCEL NO. 12: That part of the East half of the Southwest quarter of Section Twenty-three (23), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona, more particularly described as follows:

BEGINNING at the Southeast corner of the said East half of the Southwest quarter of Section 23; thence West, an assumed bearing along the South line of the said East half of the Southwest quarter of Section 23, for a distance of 762.04 feet; thence North 0 degrees 03 minutes 39 seconds West; parallel to the East line of the said East half of the Southwest quarter of Section 23, for a distance of 1946.46 feet to a point on the South right-of-way line of the 200 foot wide HASSAYAMPA-SALOME HIGHWAY, as recorded in Book 12 of Road Maps, page 82, Maricopa County Recorder, Maricopa County, Arizona; thence continuing North 0 degrees 03 minutes 39 seconds West for a distance of 234.15 feet to a point on the North right-of-way line of said highway; thence South 58 degrees 43 minutes 35 seconds East, along said North right-of-way line for a distance of 892.17 feet to a point on the said East line of the East half of the Southwest quarter of Section 23; thence South 0 degrees 03 minutes 39 seconds East, along said East line for a distance of 234.15 feet to a point on the said South right-of-way line; thence continuing South 0 degrees 03 minutes 39 seconds East for a distance of 1483.31 feet to the true point of beginning;

EXCEPT the East 305 feet of the South 305 feet thereof; and

EXCEPT one-half of the minerals and mineral rights and mineral estates of every kind and nature, as set forth in Deed recorded in Docket 11652, page 52, Maricopa County Records.

PARCEL NO. 13: The North half of the South half of the Northwest quarter of the Northwest quarter of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

EXHIBIT B
to
DEED AND
BILL OF SALE

UNIT 2 DESCRIPTION

Unit 2 of the Palo Verde Nuclear Generating Station (PVNGS), located in Maricopa County, Arizona, approximately 55 miles west of the City of Phoenix, Arizona, and approximately 16 miles west of the City of Buckeye, Arizona, consisting of:

- I. Unit 2 Combustion Engineering "System 80" pressurized water reactor nuclear steam supply system (the NSSS). The NSSS is comprised of a reactor vessel containing 241 fuel assemblies with approximately 100 tons of enriched uranium (fuel assemblies, however, are not part of Unit 2 and are not included in the Undivided Interest being sold), two steam generators, four reactor coolant pumps and various additional systems and subsystems. The licensed thermal rating of the NSSS is 3800 MW.
- II. Unit 2 GE TC6F-43, 1800 RPM tandem-compound, six flow, reheat turbine-generator including turbine, generator, moisture separator-reheater, exciter, controls, and auxiliary subsystems. The turbine-generator is conductor cooled and rated at 1,554 MVA at 24,000 V, 3 phase, 60 Hz, 1.5 in Hg ABS back pressure, and approximately 1,363 MW maximum gross electric output.
- III. Unit 2 146 ft. inside diameter, steel-lined, prestressed concrete cylindrical containment building with a hemispherical dome designed for 60 psig. The containment building houses the reactor system.
- IV. Unit 2 auxiliary systems and equipment including engineered safeguards systems, reactor auxiliary systems and turbine-generator auxiliary systems associated with items I, II, and III above, extending to and including the Unit 2 start-up transformer.
- V. Unit 2 cooling tower system consisting of three (3) mechanical draft cooling towers, including a closed cycle circulating water system, make-up water systems and essential spray ponds.

- VI. Unit 2 radioactive waste treatment system, including liquid, gaseous, and solid waste subsystems, controls, instrumentation, storage, handling and shipment facilities.
- VII. Unit 2 emergency diesel-generator system, including a diesel-generator building which contains two diesel generators, fuel oil systems, storage tanks, control and instrumentation systems and other equipment.
- VIII. Unit 2 internal communication systems, including associated interconnections and computer data links.

BUT EXCLUDING:

- I. Nuclear fuel for Unit 2, including spare fuel assemblies, and nuclear waste.
- II. Spare Parts (Unit 2).
- III. Transmission facilities (including any and all facilities and equipment providing interconnection between the Unit 2 turbine generator and the ANPP High Voltage Switchyard, including step-up transformers and standby equipment and systems).
- IV. Oil and diesel fuel inventories (Unit 2).

When recorded, return to: David Sprentall
Snell & Wilmer
3100 Valley Bank Center
Phoenix, Arizona 85073

DEED

For the consideration of Ten Dollars (\$10.00) and other valuable considerations, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (Grantor), hereby grants, conveys, sells, transfers and assigns to THE FIRST NATIONAL BANK OF BOSTON, a national banking association, as Owner Trustee (the Owner Trustee) under that certain Trust Agreement (the Trust Agreement), with the beneficiary identified below, dated as of August 1, 1986 (the Owner Trustee being hereinafter referred to as Grantee), until the commencement of Decommissioning, as such term is defined in Appendix A attached hereto, an undivided 1.74% interest in the land that is more particularly described in Exhibit A attached hereto and by this reference incorporated herein (the Land), together with all rights and privileges of Grantor appurtenant thereto, including but not limited to the perpetual (subject to the Possibility of Reversion, as hereinafter defined) right to locate, maintain and use the Improvements (as hereinafter defined) on the Land and the perpetual (subject to the Possibility of Reversion) right of ingress and egress over, upon and across the Land to the Improvements, BUT excepting and excluding from the transfer being made pursuant to this Deed any and all facilities, structures, improvements, equipment and property of whatever kind and nature now or hereafter constructed, placed or affixed on the Land (collectively, the Improvements), Grantor and Grantee hereby acknowledging and agreeing that the interest in the Improvements was acquired by Grantee pursuant to a separate Deed and Bill of Sale dated as of August 18, 1986, between Grantor and Grantee and not pursuant to this Deed.

I. The interest being transferred pursuant to this Deed is subject to the ANPP Participation Agreement (as such term is defined in Appendix A attached hereto), the Project Agreements (as defined in said ANPP

Participation Agreement), any Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition thereof in Appendix A attached hereto and to the matters set forth in Exhibit B attached hereto and incorporated herein by this reference.

II. Grantor hereby warrants that it is the true and lawful owner of the undivided interest conveyed hereby in the property described in Exhibit A attached hereto and has good right to sell the undivided interest in such property; that Grantor has good and marketable title to the undivided interest in the property described in Exhibit A and that title to such property is on the date of execution hereof free and clear of all claims, liens, encumbrances, security interests, covenants, assessments, rights, reservations, easements, restrictions and conditions save and except only any Permitted Liens described in clause (i), (v), (vi), (ix), (x) or (xi) of the definition thereof in Appendix A attached hereto and those matters set forth in Exhibit B attached hereto. Grantor hereby warrants that good and marketable title to the undivided interest in the property described in Exhibit A is hereby conveyed to Owner Trustee subject only to the Possibility of Reversion; and that the title to the undivided interest in the property described in Exhibit A conveyed to the Owner Trustee is determinable only to the extent that such title shall automatically terminate and revert to the Grantor, its successors and assigns, without any further act or deed by any person whatsoever upon the commencement of Decommissioning (such possibility of automatic termination and reversion being herein referred to as the Possibility of Reversion). Subject only to the Possibility of Reversion and to the matters set forth in Exhibit B attached hereto, Grantor hereby warrants, and will forever defend, the title against all persons whomsoever. Any attempt by Grantor, its successors and assigns, to terminate the Possibility of Reversion shall be null, void and of no force or effect whatsoever.

III. Grantor intends by this Deed that, from and after the recordation of this Deed, but subject to the Possibility of Reversion, Grantee will own an undivided 1.74% interest in the property described in Exhibit A, as a tenant in common with the owners of the remaining undivided interests in such property.

IV. Pursuant to Arizona Revised Statutes Section 33-401, the beneficiary of the Trust Agreement is Emerson Finance Co., a Delaware corporation, 111 East Prospect, Stamford, CT 06904: Attention: President. A copy of the Trust Agreement is available for inspection at the offices of the Owner Trustee at 100 Federal Street, Boston, Massachusetts 02110, Attention of Corporate Trust Division.

IN WITNESS WHEREOF, Grantor has caused this Deed to be executed as of the 18th day of August, 1986.

ARIZONA PUBLIC SERVICE
COMPANY,

an Arizona corporation

By 
Vice President and Treasurer

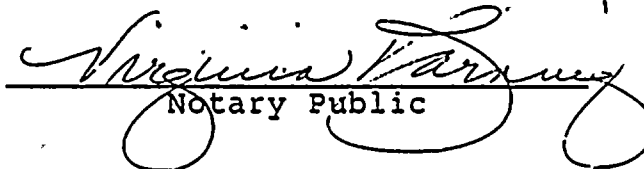
ACCEPTED AND AGREED TO:

The First National Bank of Boston,
a national banking association,
not in its individual capacity, but
solely as Trustee of the Trust
Agreement.

By 
Assistant Vice President

STATE OF NEW YORK)
) ss.
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Paul A. Williams II, Vice President and Treasurer of Arizona Public Service Company an Arizona corporation, on behalf of the corporation.

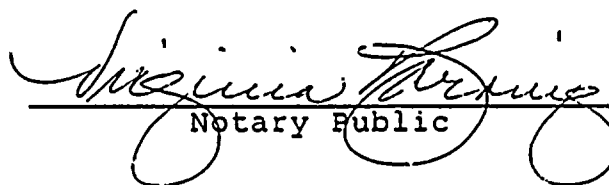

Notary Public

My Commission Expires: _____

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified in Kings County
Certificate filed in New York County
Commission Expires March 30, 1988

STATE OF NEW YORK)
) ss.
County of New York)

The foregoing instrument was acknowledged before me this 18th day of August, 1986, by Martin P. Henry, Assistant Vice President of THE FIRST NATIONAL BANK OF BOSTON, a national banking association, on behalf of the banking association as Owner Trustee under that certain Trust Agreement dated as of August 1, 1986.


Notary Public

VIRGINIA BARNING
Notary Public, State of New York
No. 24-4603310
Qualified in Kings County
Certificate filed in New York County
Commission Expires March 30, 1988

EXHIBIT A
to
DEED

PVNGS SITE DESCRIPTION

PARCEL NO. 1: Lot Four (4); the Southwest quarter of the Northwest quarter; and the West half of the Southwest quarter, all in Section Two (2), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 2: All of Section Three (3), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 3: The East half of Section Four (4), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 4: The West half of Section Twenty-six (26), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 5: Section Twenty-seven (27), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter of Section 27.

PARCEL NO. 6: The Southeast quarter of Section Twenty-eight (28), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT 50% of all oil, gas and other mineral deposits and geothermal resources recovered from or developed on the property, as reserved in instrument recorded May 10, 1974 in Docket 10647, page 136.

PARCEL NO. 7: The East half of Section Thirty-three (33), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 8: All of Section Thirty-four (34), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 9: The West half of Section Thirty-five (35), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

PARCEL NO. 10: The Southeast quarter of Section Nine (9), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the Northwest quarter thereof.

PARCEL NO. 11: All of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona; EXCEPT the East half of the Southeast quarter thereof; and EXCEPT the North half of the South half of the Northwest quarter of the Northwest quarter thereof.

PARCEL NO. 12: That part of the East half of the Southwest quarter of Section Twenty-three (23), Township One (1) North, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona, more particularly described as follows:

BEGINNING at the Southeast corner of the said East half of the Southwest quarter of Section 23; thence West, an assumed bearing along the South line of the said East half of the Southwest quarter of Section 23, for a distance of 762.04 feet; thence North 0 degrees 03 minutes 39 seconds West; parallel to the East line of the said East half of the Southwest quarter of Section 23, for a distance of 1946.46 feet to a point on the South right-of-way line of the 200 foot wide HASSAYAMPÀ-SALOME HIGHWAY, as recorded in Book 12 of Road Maps, page 82, Maricopa County Recorder, Maricopa County, Arizona; thence continuing North 0 degrees 03 minutes 39 seconds West for a distance of 234.15 feet to a point on the North right-of-way line of said highway; thence South 58 degrees 43 minutes 35 seconds East, along said North right-of-way line for a distance of 892.17 feet to a point on the said East line of the East half of the Southwest quarter of Section 23; thence South 0 degrees 03 minutes 39 seconds East, along said East line for a distance of 234.15 feet to a point on the said South right-of-way line; thence continuing South 0 degrees 03 minutes 39 seconds East for a distance of 1483.31 feet to the true point of beginning;

EXCEPT the East 305 feet of the South 305 feet thereof; and

EXCEPT one-half of the minerals and mineral rights and mineral estates of every kind and nature, as set forth in Deed recorded in Docket 11652, page 52, Maricopa County Records.

PARCEL NO. 13: The North half of the South half of the Northwest quarter of the Northwest quarter of Section Ten (10), Township One (1) South, Range Six (6) West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

EXHIBIT B
to
DEED

1. The right to enter upon, occupy and use, any part or all of that portion of the West half of the West half of Section 27, lying within 20 feet of the center line of the transmission line right of way of the Central Arizona Light and Power Company for the purposes provided in the Act of June 10, 1920 (41 STAT., 1063), and subject to the conditions and limitations of Section 24 of said Act, as amended by the Act of August 26, 1935 (49 STAT., 846), as reserved unto the United States of America in instrument recorded September 30, 1949 in Docket 442, page 577. (Part of Parcel 5 - South half of said Section 27)

2. Roadway over the South 65 feet of said Sections 9 and 10, as shown on Book 13 of Road Maps, page 48. (Parcels 10 and 11)

3. Easement and rights incident thereto for electric lines approximately 28 feet South of the North line of said Section 34, as set forth in instrument recorded February 20, 1952 in Docket 878, page 548. (Parcel No. 8)

4. All the Oil and Gas in said lands, as reserved unto the United States of America, and the right to prospect for, mine and remove such deposits from the same upon compliance with the conditions and subject to the provisions and limitations of the Act of June 17, 1914 (38 Stat. 509), as set forth in Patent recorded June 4, 1957 in Docket 2194, page 409. (Part of Parcel No. 11)

5. Easement and rights incident thereto for transmission line over said Section 34, said easement being 10 feet in width, the centerline described as follows: Beginning at a point approximately 28 feet South and 2445.5 feet East of the Northwest corner of said Section 34; thence Southerly along, parallel to and approximately 2620 feet to a point; thence Easterly along, parallel to, and approximately 2648 feet South of the North line of said Section 34, a distance of approximately 1556 feet to a point, as set forth in instrument recorded January 15, 1962 in Docket 3992, page 49. (Parcel No. 8)

6. One-Sixteenth of all gas, oil, metals and mineral rights as reserved unto the State of Arizona, in Patent recorded January 11, 1974 in Docket 10473, page 447. (Parcel 1)

7. Easement and rights incidents thereto for highway purposes over the West 55 feet of the East half of said Section 4, as set forth in the instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 3)

8. Easement and rights incident thereto for highway purposes over the West 55 feet of the Southeast quarter of said Section 28, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 6)

9. Easement and rights incident thereto for highway purposes over the West 55 feet of the East half of said Section 33, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Parcel 7)

10. Easement and rights incident thereto for highway purposes over the West 55 feet of the Southeast quarter of said Section 9, as set forth in instrument recorded October 10, 1975 in Docket 11370, page 142. (Part of Parcel 10)

11. Easement and rights incident thereto for electric lines over the North 10 feet of the following described property: The Southeast quarter of Section 28, Township 1 North, Range 6 West Except the West 55 feet thereof for roadway, as set forth in instrument recorded June 25, 1976 in Docket 11736, page 1089. (Parcel 6)

12. Easement for highway purposes over said premises, as granted to Maricopa County, a Political Subdivision, by instrument recorded December 15, 1977 in Docket 12602, page 575, described as follows: The South 40 feet of the East one-half of the Southeast quarter of Section 9; the South 40 feet of the Southwest quarter of Section 10; the South 40 feet of the West one-half of the Southeast quarter of Section 10, the South 40 feet of the Southwest quarter of the Southeast quarter of Section 9; All being in Township 1 South, Range 6 West of the Gila and Salt River Base and Meridian, Maricopa County, Arizona.

13. A roadway of a width consistent with the right of way over the Southerly portion of Sections 9 and 10 of the within described property, and other property designated County Road on Book 25 of Road Maps, page 47, recorded December 26, 1978. (Also known as Ward Road from the Hassayampa Salome Highway to the South entrance of the Palo Verde Nuclear Generating Station)

14. 1986 taxes not yet due and payable.

15. Easement and rights incident thereto for transmission line over a portion of said premises, as set forth in instrument recorded November 15, 1985 in Document No. 85-544604. (Parcels 1, 2, 8, 9 and 11)

16. Easement and rights incident thereto for highway over a portion of said premises, as set forth in instrument recorded February 3, 1959 in Docket 2740, page 309, and as shown in Book 12 of Road Maps, page 82 (Parcel 12).

17. Easement and rights incident thereto for roadway 20 feet in width, over the East 20 feet of the within described property, by instrument recorded October 19, 1976, in Docket 11907, page 115 (Parcel 12).

Appendix A

DEFINITION OF TERMS

The terms defined herein relate to the Participation Agreement (as defined below) and certain Transaction Documents executed, or to be executed, in connection with the Participation Agreement. Such terms include the plural as well as the singular. Any agreement defined or referred to below shall include each amendment, modification and supplement thereto and waiver thereof as may become effective from time to time, except where otherwise indicated. Any term defined below by reference to any agreement shall have such meaning whether or not such document is in effect. The terms "hereof", "herein", "hereunder" and comparable terms refer to the entire agreement with respect to which such terms are used and not to any particular article, section or other subdivision thereof.

If, and to the extent that, either the Participation Agreement or any other Transaction Document which incorporates this Appendix shall be amended from time to time pursuant to the respective terms thereof, this Appendix shall be, or be deemed to have been, amended concurrently with the execution and delivery of each such amendment in order to conform the definitions herein to the new or amended definitions set forth in or required by each such amendment.

Additional Bonds shall mean Bonds in addition to the Initial Series Bonds.

Additional Equity Investment shall have the meaning set forth in Section 8(f) of the Facility Lease.

Additional Notes shall have the meaning set forth in the recitals to the Indenture, which Additional Notes shall be issued, if at all, pursuant to Section 3.5 of the Indenture.

Adjusted Base Amount shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Affiliate, with respect to any Person, shall mean any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person. For purposes of this definition, the term "control" (including the correlative meanings of the terms "controlled by" and "under common control with"), as used with respect to any Person, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management policies of such Person, whether through the ownership of voting securities or by contract or otherwise.

After-Tax Basis shall mean, with respect to any payment received or deemed to have been received or accrued by any Person, the amount of such payment supplemented by a further payment to that Person so that the sum of the two payments shall, after deduction of all taxes and other charges (taking into account any credits or deductions arising therefrom and the timing thereof) computed at the highest marginal statutory tax rate resulting from the receipt (actual or constructive or accrued) of such two payments imposed under any Applicable Law or by any Governmental Authority, be equal to such payment received or deemed to have been received or accrued.

Agent shall mean Bank of America, as Agent for the Original Loan Participants under the Bank Agency Agreement.

Agency Period shall have the meaning set forth in Section 7.01 of the Assignment and Assumption.

ANPP Administrative Committee shall mean the committee established pursuant to Section 6.1.1 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Operating Committee shall mean the committee established pursuant to Section 6.1.2 of the ANPP Participation Agreement (or any comparable successor provision).

ANPP Participants shall have the meaning assigned to the word "Participant" under the ANPP Participation Agreement.

ANPP Participation Agreement shall mean the Arizona Nuclear Power Project Participation Agreement, dated as of August 23, 1973, among APS, Salt River, Southern California, PNM, El Paso, SCPPA and LADWP.

ANPP Project Agreements shall mean the ANPP Participation Agreement and the other Project Agreements (as such term is defined in the ANPP Participation Agreement).

ANPP Switchyard shall mean the ANPP High Voltage Switchyard located at the PVNGS Site, the ownership, construction, operation and maintenance of which are governed by the ANPP High Voltage Switchyard Participation Agreement executed as of August 20, 1981 (APS Contract No. 2252-419,00), the parties to which are PNM, APS, Salt River, El Paso, LADWP and Southern California.

Applicable Law shall mean all applicable laws, statutes, treaties, rules, codes, ordinances, regulations, permits, certificates, orders, interpretations, licenses and permits of any Governmental Authority and judgments, decrees, injunctions, writs, orders or like action of any court, arbitrator or other judicial or quasi-judicial tribunal (including those pertaining to health, safety, the environment or otherwise).

Appraisal Procedure shall mean a procedure whereby two independent appraisers, one chosen by the Lessee and one by the Lessor, shall mutually agree upon the value, period, amount or determination then the subject of an appraisal. If either the Lessor or the Lessee, as the case may be, shall determine that a value, period, amount or determination to be determined under the Facility Lease or any other Transaction Document cannot timely be established by mutual agreement, such party shall appoint its appraiser and deliver a written notice thereof to the other party. Such other party shall appoint its appraiser within 30 days after receipt from the other party of the foregoing written notice. If within 60 days after appointment of the two appraisers, as described above, the two appraisers are unable to agree upon the value, period, amount or

determination in question, a third independent appraiser shall be chosen within ten days thereafter by the mutual consent of such first two appraisers or, if such first two appraisers fail to agree upon the appointment of a third appraiser within such period, such appointment shall be made by the American Arbitration Association, or any organization successor thereto. The decision of the third appraiser so appointed and chosen shall be given within 60 days after the selection of such third appraiser. If three appraisers shall be so appointed and the determination of one appraiser is more disparate from the middle determination by more than twice the amount by which the third determination is disparate from the middle determination, then the determination of such appraiser shall be excluded, the remaining two determinations shall be averaged and such average shall be binding and conclusive on the Lessor and the Lessee; otherwise the average of all three determinations shall be binding and conclusive on the Lessor and the Lessee. The fees and expenses of appraisers incurred in connection with any Appraisal Procedure relating to any transaction contemplated by any provision of any Transaction Document shall be divided equally between the Lessor and the Lessee (except pursuant to Sections 14(a) or 16 of the Facility Lease or for purposes of determining the Maximum Option Period, which shall be paid solely by the Lessee).

APS shall mean Arizona Public Service Company, an Arizona corporation.

Arizona Corporation Commission shall mean the Arizona Corporation Commission established pursuant to Article XV, Section 1 of the Constitution of the State of Arizona.

Arizona Order shall mean the Order of the Arizona Corporation Commission, Decision No. 55120, dated July 24, 1986.

Arizona Public Utility Act shall mean Chapter 2 of Title 40, Arizona Revised Statutes.

Assigned Payments shall have the meaning specified in Section 2.1(2) of the Indenture.

Assignment and Assumption shall mean the Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and the Owner Trustee.

Assumption Agreement shall mean the Assumption Agreement of APS substantially in the form of Exhibit B to the Indenture.

Assumptions shall mean the Pricing Assumptions and the Tax Assumptions.

Atomic Energy Act shall mean the Atomic Energy Act of 1954, as amended.

Authorized Officer shall mean, with respect to the Indenture Trustee, any officer of the Indenture Trustee or any other Person who shall be duly authorized by appropriate corporate action on the part of the Indenture Trustee to authenticate a Note and shall mean, with respect to the Owner Trustee, any officer of the Owner Trustee who shall be duly authorized by appropriate corporate action to execute any Transaction Document.

Bank Agency Agreement shall mean the agency agreement, dated as of August 14, 1986, among the Agent and the Original Loan Participants.

Bank of America shall mean Bank of America National Trust and Savings Association, a national banking association.

Bank Exchange Note shall have the meaning set forth in Section 3.9(b) of the Indenture.

Bankruptcy Code shall mean the Bankruptcy Reform Act of 1978, as amended, and any law with respect to bankruptcy, insolvency or reorganization successor thereto.

Basic Lease Term shall mean the initial term of the Facility Lease, which shall begin on the Closing Date and end on December 31, 2015, unless earlier terminated as provided in the Facility Lease.

Basic Rent shall have the meaning set forth in Section 3(a) of the Facility Lease.

Basic Rent Payment Dates shall mean and include June 30, 1987, and each June 30 and December 30 thereafter, commencing June 30, 1987 and ending December 30, 2015, and, if the Lessee shall elect one or more Renewal Terms, each June 30 and December 30 of each year during each Renewal Term.

Bill of Sale shall mean the Deed and Bill of Sale, dated August 18, 1986, between APS and the Owner Trustee.

Bonds shall mean all bonds, notes and other evidences of indebtedness from time to time issued and outstanding under any Collateral Trust Indenture.

Business Day shall mean any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York, Boston, Massachusetts or San Francisco, California are authorized or obligated to be closed.

Capital Improvement shall mean (a) the addition, betterment or enlargement of any property constituting part of Unit 2 or the replacement of any such property with other property, irrespective of whether (i) such replacement property constitutes an enlargement or betterment of the property which it replaces, (ii) the cost of such addition, betterment, enlargement or replacement is or may be capitalized, or not charged to maintenance or repairs, in accordance with the Uniform System of Accounts or (iii) such addition, betterment or enlargement, is or is not included or reflected in the plans and specifications for Unit 2, as built, and (b) any alteration, modification, addition or improvement to Unit 2, other than original, substitute or replacement parts incorporated into Unit 2.

Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of

the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any Basic Rent Payment Date, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Change in Tax Law shall have the meaning set forth in Section 3(d) of the Facility Lease.

Chemical Bank or Chemical shall mean Chemical Bank, a New York banking corporation.

Chief Financial Officer shall mean with respect to a Person, the individual designated by the Board of Directors of such Person as the chief financial officer of such Person.

Claims shall mean liabilities, obligations, losses, damages, Taxes (other than Taxes on income), penalties, claims (including, without limitation, claims involving liability in tort, strict or otherwise), actions, suits, judgments, costs, interest, expenses and disbursements, whether or not any of the foregoing shall be founded or unfounded (including, without limitation, legal fees and expenses and costs of investigation) of any kind and nature whatsoever without any limitation as to amount.

Closing shall mean the proceedings which occur on the Closing Date, as contemplated by the Participation Agreement.

Closing Date shall mean August 18, 1986.

Closing Date Transaction Expenses shall have the meaning set forth in Section 5(a) of the Participation Agreement.

Code shall mean the Internal Revenue Code of 1954, as amended, or any comparable successor law.

Collateral Trust Indenture shall mean a Collateral Trust Indenture among APS, Funding Corp and the Collateral Trust Trustee in form and substance satisfactory to APS, Funding Corp and the Collateral Trust Trustee.

Collateral Trust Indenture Supplement shall mean a supplement to the Collateral Trust Indenture.

Collateral Trust Trustee shall mean Chemical Bank, not in its individual capacity, but solely as Collateral Trust Trustee under the Collateral Trust Indenture, and the successors or assigns of such Trustee.

Common Facilities shall mean all PVNGS common facilities which are common to all generating units, including Unit 2, at PVNGS.

Cure Option shall have the meaning set forth in Section 16(e) of the Facility Lease.

Debt shall mean (A) secured or unsecured indebtedness for borrowed money or for the deferred purchase price of property or evidenced by notes, bonds or other instruments, (B) obligations as lessee under capital leases, (C) the present value of obligations as lessee under other leases the remaining term of which (including options to renew) is more than one year, in each case discounted to present value as of the respective dates on which such obligations are due at the rate per annum borne by the debt placed in conjunction with such lease or, if no such debt was placed, at the Lessee's marginal cost of debt at the time such lease was entered into, (D) obligations secured by any Lien existing on any property owned or held by a Person, whether or not such Person has assumed or become liable for the obligations secured thereby, and (E) obligations under direct or indirect guarantees of (including obligations (contingent or otherwise) to assure a creditor against loss in respect of) indebtedness or obligations of others of the kinds referred to in clause (A), (B), (C) or (D) above. For purposes of the foregoing, there shall be excluded obligations under any operating lease of computers, office equipment or the like, the original

term of which (including options to renew) is less than five years.

Decommissioning shall have the meaning in respect of Unit 2 and the Unit 2 Retained Assets (including, without limitation, the Common Facilities and the PVNGS Site allocable to Unit 2) set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Cost shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trust Agreement shall mean the Decommissioning Trust Agreement, among the Owner Trustee, the Lessee and the Decommissioning Trustee.

Decommissioning Trust Fund shall have the meaning set forth in Section 10(b)(3)(viii) of the Participation Agreement.

Decommissioning Trustee shall mean Bankers Trust Company, a New York trust company, as decommissioning trustee under the Decommissioning Trust Agreement, and each successor decommissioning trustee under such Agreement.

Decommissioning Fund Permitted Investments shall have the meaning set forth in Exhibit A to the Decommissioning Trust Agreement.

DECON shall mean the decommissioning alternative in which the equipment, structures and portions of a facility and site containing radioactive contaminants are removed or decontaminated to a level that permits the property to be released for unrestricted use shortly after cessation of operations.

Deemed Loss Events shall mean [to be supplied by amendment].

Default shall mean an event or condition which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

Directive shall mean an instrument in writing executed in accordance with the terms and provisions of the Indenture by the Holders, or their duly authorized agents or attorneys-in-fact, representing a Majority in Interest of Holders of Notes, directing the Indenture Trustee to take or refrain from taking the action specified in such instrument or otherwise advising the Indenture Trustee; provided, however, that each Holder of Notes then Outstanding, or its duly authorized agent or attorney-in-fact, shall be entitled to direct the Indenture Trustee as herein provided only with respect to the aggregate unpaid principal amount of Notes (or portion thereof) issued and Outstanding which are registered in the name of such Holder and which are certified by such Holder or its duly authorized agent or attorney-in-fact to be (i) held by it for its own account and not pledged as collateral for any of its obligations or (ii) pledged as collateral for one or more of its obligations, or obligations with respect to which it is acting as trustee under a related indenture, but in respect of which it has received a directive, satisfactory in form and substance to the Indenture Trustee, given by the holder or holders of a proportionate interest in the obligations secured by such Notes in accordance with the instrument governing such obligations. More than one direction can be given by a registered Holder of Notes or its duly authorized agent or attorney-in-fact pursuant to clause (ii) of the preceding sentence, and such directions may be contradictory or inconsistent, so long as each direction to take or refrain from taking the action specified therein or otherwise advising the Indenture Trustee meets the requirements of said clause (ii).

Eligible Bank shall mean a commercial bank, trust company in the nature of a bank or United States branch or agency of a foreign bank with deposits in the United States in excess of \$500,000,000 which is a member of the Federal Reserve Bank (as used herein, an Issuing Bank) not related to the Equity Participant or the Lessee at the time of issuance of any Letter of Credit which shall be (i) Morgan Bank, so long as its long-term unsecured debt securities shall be rated not less than Aa3 by Moody's, (ii) any Issuing Bank whose long-term unsecured debt securities are rated Aaa by Moody's, unless there are legal or regulatory constraints on the issuance to or holding by the Equity Participant of a letter of credit from such Issuing Bank, or (iii) any Issuing Bank whose long-term

unsecured debt securities and the long-term unsecured debt securities of any parent company of such Issuing Bank are rated not less than Aa3 by Moody's, other than an Issuing Bank to which the Equity Participant shall not consent (such consent not to be unreasonably withheld, it being understood that one of the bases for withholding such consent may be, in the case of an Issuing Bank which is part of a holding company structure, the failure of such Issuing Bank's parent holding company to have a rating not less than Aa3 by Moody's in respect of its long-term unsecured debt securities but eligibility under this clause (iii) shall not be available if the cost of a Letter of Credit issued by an Issuing Bank otherwise qualifying under clause (i) or (ii) for a period of five years shall be greater than the cost of the prior Letter of Credit provided by an Eligible Bank qualifying under clause (i) or (ii); provided, however, that any Letter of Credit issued by an Issuing Bank that is not incorporated in the United States shall provide that all payments shall be in United States dollars and shall be made in New York, New York or such other city in the United States as the Equity Participant shall reasonably request.

El Paso shall mean El Paso Electric Company, a Texas corporation.

Equity Participant shall mean Emerson Finance Co., and its successors and assigns in accordance with the Trust Agreement and the Participation Agreement.

Equity Participant's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, the Equity Participant unrelated to the transactions contemplated by the Transaction Documents.

Equity Portion of Rent shall mean (i) in the case of any payment of Basic Rent, the amount of Basic Rent payable under the Facility Lease reduced by the principal and interest then due and payable on the Notes, (ii) in the case of any payment of Casualty Value, Special Casualty Value or Extraordinary Casualty Value, the amount thereof reduced by the principal amount of and accrued interest on the Outstanding Notes

or (iii) in the case of any payment of Supplemental Rent, the amount thereof payable to the Owner Participant.

ERISA shall mean the Employee Retirement Income Security Act of 1974, as amended.

Event of Default shall have the meaning set forth in Section 15 of the Facility Lease.

Event of Loss shall mean any of the following events: (a) a Final Shutdown; (b) a Requisition of Title; or (c) a Requisition of Use.

Excepted Payments shall mean [to be supplied by amendment].

Excepted Rights shall mean all rights with respect to Excepted Payments of the Person entitled thereto and interest with respect to (i) the Decommissioning Trust Fund and all payments by the Lessee thereunder or in respect of Decommissioning, and (ii) the Letter of Credit and any amounts paid or payable under the Letter of Credit.

Excess Amount shall have the meaning set forth in Section 19(f) of the Participation Agreement.

Existing Mortgage shall mean the Mortgage and Deed of Trust, dated as of July 1, 1946, between APS and Security Pacific National Bank, together with thirty-seven indentures supplemental thereto.

Extraordinary Casualty Value, as of any Basic Rent Payment Date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 5 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining as a residual the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Extraordinary Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(c) of the

Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any Basic Rent Payment Date, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Facility Cost shall mean the Purchase Price plus the sum of (x) all Supplemental Financing Amounts and (y) all Additional Equity Investment amounts.

Facility Lease shall mean the Facility Lease, dated as of August 1, 1986, between APS, as Lessee, and the Owner Trustee, as Lessor.

Fair Market Renewal Term shall have the meaning set forth in Section 12(b) of the Facility Lease.

Fair Market Rental Value or Fair Market Sales Value of any property or service shall mean the value, which shall not in any event be less than zero, of such property or service for lease or sale determined on the basis of an arm's-length transaction for cash between an informed and willing lessee or buyer or purchaser (under no compulsion to lease or purchase) and an informed and willing lessor or seller (under no compulsion to lease or sell), and shall take into account the Lessor's rights and obligations under the Assignment and Assumption, but shall be without regard to any rights of the Lessee (including any Renewal Option) under the Facility Lease, including (except for purposes of Section 16 of the Facility Lease) in such value the Decommissioning Trust Fund and the existence of the rights afforded by Section 10(b)(3)(viii) of the Participation Agreement to the parties identified therein. Except pursuant to Section 16 (other than Section 16(e)) of the Facility Lease or Section 6.01 of the Assignment and Assumption, Fair Market Rental Value and Fair Market Sales Value of the Undivided Interest and the Real Property Interest shall be determined on the assumption that (i) Unit 2 has been maintained in accordance with, and the Lessee has complied with, the requirements of the Facility Lease and the other Transaction Documents and the ANPP Participation Agreement, and (ii) the Lessee is otherwise in compliance with the requirements of all Transaction Documents. Fair Market Rental Value shall be determined on the assumption that basic rent will be payable in equal semi-annual installments in arrears.

Federal Power Act shall mean the Federal Power Act, as amended.

Federal Securities shall have the meaning set forth in Section 2.4(c) of the Indenture.

FERC shall mean the Federal Energy Regulatory Commission of the United States of America or any successor agency.

Final Shutdown shall mean the occurrence of any of the following:

(1) the expiration or revocation of the License or that portion of the License that permits the operation of Unit 2 or the expiration, suspension or revocation of the License or that portion of the License that permits the possession by the Lessee of the Undivided Interest and the Real Property Interest;

(2) (x) (A) the suspension of the License or that portion of the License which permits operation of Unit 2, which suspension remains in effect for three consecutive calendar months; or (B) any order of or direction (or series of orders or directions) by the NRC or any other Governmental Authority that Unit 2 suspend operations for reasons of radiological health and safety for a Period which will exceed 24 months or (y) any cessation of operation of Unit 2 for a Period of 24 months if the resumption of operations requires the concurrence of the NRC or any other Governmental Authority;

(3) the occurrence of a Nuclear Incident at Unit 2 as a result of which Unit 2 ceases to operate (or if Unit 2 is not in operation immediately prior to such Nuclear Incident, the failure to resume operation as a result of such Nuclear Incident) for a Period of 18 consecutive months;

(4) the occurrence of an event at Unit 2 as a result of which (w) the radiation level in the containment vessel of Unit 2 as measured by the average of two high range radiation monitors in the top half of such containment vessel (or if only one such monitor is operating at such time, such monitor) averaged over one hour equals or exceeds 200 rad per hour; or (x) any measure of radioactivity in the

primary coolant system of Unit 2 shall exceed by 100 times the limiting conditions for operation specified in the technical specifications for Unit 2 (as in effect on the Closing Date); or (y) any three valid core exit thermocouples shall reach a temperature in excess of 1300 degrees Fahrenheit; or (z) assessment of core damage according to PVNGS Procedures No. EPIP-14A and 74CH-9ZZ47 (as in effect on the Closing Date), using independent assessments based on any one of the following: (i) one or more readings of high-range radiation monitors located inside and/or outside of Unit 2 containment (as specified in PVNGS Procedures No. EPIP-14A, as in effect on the Closing Date) (or, if such Procedures shall be amended to provide for additional monitors located inside and/or outside of Unit 2, such additional monitors); (ii) radiochemical analysis of samples of the primary coolant water, the water in the containment sump, and the air in the containment; (iii) measurements of the concentrations of hydrogen in samples of the primary coolant water and the containment atmosphere; or (iv) measured temperatures of the valid core exit thermocouples, which indicate that the damage to the nuclear fuel residing in the reactor vessel is in categories 4, 6, 7, 8 (only for releases greater than 1% of source inventory), 9, or 10 of Appendix L to PVNGS Procedure No. 74CH-9ZZ47 as in effect on the Closing Date;

(5) the occurrence at Unit 2 of a discharge or dispersal of radioactive material off-site when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement, in amounts off-site, or causing radiation levels off-site, which (x) the NRC declares to be an Extraordinary Nuclear Occurrence (as such term is defined in the Atomic Energy Act); (y) results in off-site surface radiation levels measured over a contiguous or non-contiguous area of 100 square meters of (A) alpha particles from transuranic isotopes in excess of .35 microcuries per square meter (B) alpha particles from all other isotopes in excess of 3.5 microcuries per square meter or (C) either beta or gamma particles in excess of 4 millirads per hour as measured at a height of one centimeter (measured through not more than 7 milligrams per square centimeter of total absorber), or such alternative standards as

may hereafter be adopted by the NRC with respect to the radiation levels required for the occurrence of an Extraordinary Nuclear Occurrence and determined by the Lessee and the Equity Participant to be equivalent to the standards which were applicable hereunder prior to the adoption by the NRC of such alternative standards; provided, however, that if the NRC shall reduce any level of measurement, if either the Extraordinary Nuclear Occurrence Criteria for off site contamination are reduced by NRC as set forth above or alternative criteria are adopted by NRC, then the levels herein shall be reduced or modified so as to be consistent with the reduction by the NRC; or (2) results in on-site surface radiation levels (measured at a distance of not less than one-half mile from the outside of any building at PVNGS and over a contiguous or non-contiguous area of 100 square meters) which are in excess of 20 times the measurement level set forth in or established pursuant to clause (y) for any particle;

(6) the occurrence at Unit 2 of a discharge or dispersal of radioactive material when, as a result of an event comprised of one or more related happenings, radioactive material is released from its intended place of confinement in amounts off-site resulting in an aggregate cost of decontamination, estimated to be in excess of \$10,000,000;

(7) the declaration by the Operating Agent of a site area emergency set forth in the PVNGS Emergency Plan for any reason other than a drill or false alarm;

(8) except as a result of controlled movement of spent fuel into or within the spent fuel storage facility for Unit 2, the radiation level in the fuel building above such storage facility, as measured by a valid radiation measuring instrument located in such building above such storage facility, shall be more than 1,000 times the average of the previous five readings of such measuring instrument over a period of not less than 24 hours;

(9) damage to Unit 2 and the failure of the Lessee, or of the Lessee and one or more other ANPP Participants to complete restoration or reconstruction of Unit 2 within three years of such damage, or in the case of damage occurring less than

three years prior to the date of expiration of the Lease Term, on or before the expiration of the Lease Term;

(10) damage to Unit 2 and the failure by the Lessee within 18 months to agree to participate in the reconstruction of Unit 2;

(11) the cessation of operation of Unit 2 as a result of damage to Unit 2 for a Period which will exceed three years or end after the expiration of the Lease Term (including any then elected Renewal Term) (it being understood that the cessation of operation shall be attributable to damage to Unit 2 if such cessation shall occur within 10 days of such damage); and

(12) the destruction of Unit 2.

For purposes of this definition, a Final Shutdown declared in consequence of the occurrence of an event described in (A) clauses 3 and 4 above shall be deemed to have occurred immediately upon the occurrence of any of the following: (i) the water level within the reactor vessel shall decline to a level which is three feet above the nuclear core, (ii) the water level within the spent fuel storage facility shall decline to a level which is three feet above the top of any fuel which has been in the reactor core within the prior 12 months, (iii) the pressure within the primary coolant system shall decrease by in excess of 1000 pounds per square inch in a period of less than 5 minutes or (iv) the departure from nucleate boiling ratio shall be less than 0.9, and (B) clause 7 above shall be deemed to have occurred immediately if the water level within the spent fuel storage facility declines to a level which is three feet above any fuel which has been in the reactor core within the prior 12 months:

Financing Documents shall mean the Collateral Trust Indenture and the Underwriting Agreement.

Fixed Rate Renewal Term shall have the meanings set forth in Section 12(a) of the Facility Lease.

FNB shall mean The First National Bank of Boston, in its individual capacity, and its successors and assigns.

Form U-7D shall mean the certificate to be filed pursuant to Rule 7(d) of the Holding Company Act for the purpose of exempting the Equity Participant and the Owner Trustee from registration under the Holding Company Act.

Funding Corp shall mean PVNGS Funding Corp., Inc., a Delaware corporation.

Generating Unit shall mean Unit 1, 2 or 3 or any of the other Generating Units (as such term is defined in the ANPP Participation Agreement) constituting PVNGS.

Generation Entitlement Share shall have the meaning assigned thereto in the ANPP Participation Agreement and (i) when used in reference to Unit 2, the Generation Entitlement Share of APS as the ANPP Participant with respect to its 29.1% interest in Unit 2, (ii) when used in reference to the Undivided Interest, shall mean the Generation Entitlement Share attributable to a Unit 2 Interest in Unit 2, and (iii) when used in Section 19 of the Facility Lease, shall refer to all Generating Units at PVNGS.

Governmental Action shall mean all authorizations, consents, approvals, waivers, exceptions, variances, orders, licenses, exemptions, publications, filings, notices to and declarations of or with any Governmental Authority (other than routine reporting requirements the failure to comply with which will not affect the validity or enforceability of any of the Transaction Documents or have a material adverse effect on the transactions contemplated by any Transaction Document) or any other action in respect of any Governmental Authority and shall include, without limitation, all sitting, environmental and operating permits and licenses which are required for the use and operation of Unit 2, including the Undivided Interest and the Real Property Interest.

Governmental Authority shall mean any Federal, state, county, municipal, foreign, international, regional or other governmental authority, agency, board, body, instrumentality or court.

Granting Clause Documents shall have the meaning specified in Section 2.1(2) of the Indenture.

Holders shall mean the holders of the Notes or the Bonds, as the context may require.

Holding Company Act shall mean the Public Utility Holding Company Act of 1935, as amended.

Income/Capital Taxes shall have the meaning set forth in Section 13(b)(2)(ii) of the Participation Agreement.

Indemnatee shall mean the Equity Participant, the Owner Trustee, FNB, the Loan Participant (including each Bank), Funding Corp, the stockholder of Funding Corp and its officers and directors, Chemical Bank, the Indenture Trustee, each Holder of a Note from time to time Outstanding, the Collateral Trust Trustee, the Trust, the Trust Estate, the Lease Indenture Estate, the indenture estate under the Collateral Trust Indenture, any Affiliate of any of the foregoing and the respective successors, assigns, agents, officers, directors or employees of the foregoing, excluding, however, any ANPP Participant other than the Owner Trustee or the Equity Participant.

Indenture shall mean the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Owner Trustee and Chemical Bank.

Indenture Default shall mean an event which, after giving of notice or lapse of time, or both, would become an Indenture Event of Default.

Indenture Event of Default shall mean any of the events specified in Section 6.2 of the Indenture.

Indenture Trustee shall mean Chemical Bank, a New York banking corporation, not in its individual capacity, but solely as Indenture Trustee under the Indenture and each successor trustee and co-trustee thereunder.

Indenture Trustee's Liens shall mean Liens against the Lease Indenture Estate which result from acts of, or any failure to act by, or as a result of claims against, the Indenture Trustee, in its individual capacity, unrelated to the transactions contemplated by the Transaction Documents.

Indenture Trustee's Office shall mean the office of the Indenture Trustee located at 55 Water Street, New York, New York 10041, or such other office as may be designated by the Indenture Trustee to the Owner Trustee and each Holder of a Note Outstanding under the Indenture.

Initial Series Notes shall mean the non-recourse promissory notes, substantially in the form of Exhibit A to the Indenture, to be issued by the Owner Trustee and authenticated by the Indenture Trustee on the Closing Date to finance a portion of the Purchase Price and the Bank Exchange Notes.

Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Investment Account shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Investment Company Act shall mean the Investment Company Act of 1940, as amended.

Investment Percentage shall mean the percentage identified as such in Schedule 3 to the Participation Agreement.

IRS shall mean the Internal Revenue Service of the United States Department of the Treasury or any successor agency.

LADWP shall mean the Department of Water and Power of The City of Los Angeles, a department organized and existing under the charter of the City of Los Angeles, a municipal corporation of the State of California.

Lease Indenture Estate shall have the meaning set forth in Section 2.1 of the Indenture.

Lease Term shall mean the aggregate of the Basic Lease Term and each Renewal Term, if any.

Lease Termination Date shall mean the last day of the Lease Term (whether occurring by reason of a termination or expiration of the Lease Term).

Lessee shall mean Arizona Public Service Company, an Arizona corporation, and its successors and assigns, as lessee under the Facility Lease and as party to the other Transaction Documents to which it is a signatory.

Lessor shall mean the Owner Trustee, as lessor under the Facility Lease, and its successors and assigns.

Lessor's Interest shall have the meaning set forth in Section 8(c)(3) of the Participation Agreement.

Lessor's Liens or Owner Trustee's Liens shall mean Liens against the Trust Estate or the Lease Indenture Estate (other than Permitted Liens, except "Lessor's Liens" and "Equity Participant's Liens" referred to in clause (vi) of the definition thereof) for which the Lessee is not responsible and which result from acts of, or any failure to act by, or as a result of claims against, FNB or the Lessor, unrelated to the ownership of the Undivided Interest or to the Real Property Interest, the administration of the Trust Estate or the transactions contemplated by the Transaction Documents.

Lessor's Portion shall mean that portion of APS's interest in Unit 2 equal to the percentage set forth on Schedule 3 to the Participation Agreement.

Letter of Credit shall have the meaning set forth in Section 10(b)(3)(ix) of the Participation Agreement.

License shall mean NRC Facility Operating License No. NPF-51, issued April 24, 1986 (superseding NRC Facility Operating License No. NPF-46, issued on December 9, 1985), as the same may be amended, modified, extended, renewed or superseded from time to time.

License Amendment shall mean Amendment No. 4, dated August 15, 1986, amending the License and approving the transactions contemplated by the Participation Agreement and the Facility Lease.

License Expiration Date shall mean December 9, 2025, or such later or earlier date as the License shall expire or be terminated.

Lien shall mean any mortgage, pledge, security interest, encumbrance, lien, easement, servitude or charge of any kind, including, without limitation, any conditional sale or other title retention agreement, any lease in the nature thereof or the filing of, or agreement to give, any financing statement under the Uniform Commercial Code of any jurisdiction.

Loan shall have the meaning set forth in Section 2(a) of the Participation Agreement.

Loan Participants shall mean the Agent, on behalf of the Original Loan Participants, so long as the Initial Series Notes are Outstanding, and each Holder of a Refunding Note from time to time.

Loan Percentage shall mean, in respect of each Original Loan Participant, the percentage set forth opposite the name of such Original Loan Participant in Schedule 1 to the Participation Agreement.

Majority in Interest of Holders of Notes shall mean Holders of a majority in principal amount of all Notes Outstanding under the Indenture at the time of any such determination; provided, however, that for purposes of any determination with respect to the Initial Series Notes, such term shall mean Holders of not less than 67% in principal amount at the time of such determination.

Material Project Agreements shall mean (i) the ANPP Participation Agreement, (ii) Nuclear Fuel Contract between ANPP and Combustion Engineering, Inc. (CE), dated as of August 20, 1973, (iii) Nuclear Steam Supply Contract between APS and CE, dated as of August 20, 1973, (iv) Turbine Generator Contract between APS and General Electric Company, dated as of March 21, 1974, as amended, (v) Uranium Enrichment Services Contract between the United States of America (USA) and APS, dated November 15, 1984, as amended, and the

Associated Supplemental Agreement of Settlement between USA and APS, dated November 15, 1984, (vi) Contract between APS and Westinghouse Electric Corporation for fuel fabrication services for reload of batches of nuclear fuel, dated August 7, 1974, as amended, (vii) Agreement for the Sale and Purchase of Waste Water Effluent between the City of Tolleson, APS and Salt River, dated June 12, 1981, as amended, (viii) Agreement for Construction of ANPP between Bechtel Power Corporation (Bechtel) and APS, dated January 15, 1973, (ix) Agreement for Engineering and Procurement Services between APS and Bechtel, dated January 15, 1973, (x) Option and Purchase of Effluent, among the Cities of Phoenix, Glendale, Mesa, Tempe and Scottsdale, the Town of Youngtown, APS and Salt River dated April 23, 1973, (xi) Agreement for Conversion Services between Allied Chemical Corporation and APS, dated November 17, 1975, as amended, (xii) Uranium Concentrate Sales Agreement between Energy Rules Exploration Company and APS, dated as of December 1, 1983, (xiii) Uranium Concentrate Sales Agreement between Energy Fuels Exploration Company and APS, dated as of October 23, 1981, as amended, (xiv) Agreement for Sale of Uranium Concentrates between Pathfinder Mines Corporation and APS, dated December 1, 1983, and (xv) Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste between USA and APS, dated July 21, 1984.

Maximum Option Period shall mean the period determined as provided in Section 13(a) of the Facility Lease, in no event ending after the License Expiration Date, (i) at the end of which the residual value of the Undivided Interest shall be equal to the greater of (x) 20% of Facility Cost (without regard to inflation or deflation from the Closing Date) and (y) 20% of the then determined Fair Market Sales Value of the Undivided Interest (without regard to inflation or deflation from the beginning of such Fixed Rate Renewal Term) in each case determined by taking into consideration the obligation of the Lessee to pay the portion of Decommissioning Cost attributable to the period following the end of the Basic Lease Term pursuant to Section 10(b)(3)(viii) of the Participation Agreement, and the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets, (ii) which, when added to the Basic Lease Term, does not exceed 80% of the economic useful life of the Undivided Interest from the Closing Date and

(iii) at the end of which, taking into consideration the existence and effect of the Assignment and Assumption, the ANPP Project Agreements, the License and any additional expenditure that would be required to acquire the Unit 2 Retained Assets, the use of the Undivided Interest by any User (in a transaction pursuant to which the Equity Participant could realize the amount referred to in clause (i) above) is feasible from an engineering and economic point of view and is commercially reasonable. Unless the period, as computed in accordance with the preceding sentence, shall end on a June 30 or December 31 of any year, the final date of the Maximum Option Period shall be the final June 30 or the December 30 in the last twelve months of such period, as so computed.

Modified Special Casualty Value, as of any date, shall mean the percentage of Facility Cost set forth opposite such date in Schedule 4 to the Facility Lease.

Moody's shall mean Moody's Investors Service, Inc., and any successor issuing nationally accepted securities ratings.

Morgan Bank shall mean Morgan Guaranty Trust Company of New York, a New York trust company, and its successors and assigns.

Mortgage Release shall mean the Partial Release, dated as of the Closing Date, under and with respect to the Existing Mortgage.

Net Economic Return shall mean the after-tax yield and after-tax cash flow originally expected by the Equity Participant with respect to the Undivided Interest, calculated utilizing the Assumptions and the initial computation of Basic Rent, Casualty Value, Special Casualty Value, Modified Special Casualty Value and Extraordinary Casualty Value derived from the Assumptions.

Net Worth shall mean consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied.

Non-Burdensome Regulation shall mean (i) regulation to which the Equity Participant or the Owner Trustee is otherwise subject by reason of its lease financing or other activities unrelated to the transactions contemplated by the Transaction Documents, (ii) ministerial regulatory requirements which do not impose limitations or regulatory requirements on the business or activities of the Equity Participant and which are deemed, in the reasonable discretion of the Equity Participant, not to be burdensome, (iii) assuming redelivery of the Undivided Interest in accordance with Section 5(a) of the Facility Lease, regulation resulting from any possession of the Undivided Interest on or after the Lease Termination Date or (iv) regulation of the Owner Trustee which would be terminated by the appointment of a successor Owner Trustee or a co-Owner Trustee pursuant to the terms of the Trust Agreement.

Nonseverable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which is not a Severable Capital Improvement.

Noteholder shall mean any Holder from time to time of a Note Outstanding under the Indenture.

Notes shall mean all Initial Series Notes, Refunding Notes and Additional Notes issued from time to time in registered form under the Indenture.

Notice of Closing shall have the meaning set forth in Section 5(a) of the Participation Agreement.

NRC shall mean the Nuclear Regulatory Commission of the United States of America or any successor agency.

Nuclear Incident shall have the meaning set forth in the Atomic Energy Act; provided that if the Atomic Energy Act shall be amended after the date hereof to expand the definition of "nuclear incident", the meaning of Nuclear Incident shall be similarly expanded.

Nuclear Waste Act shall mean the Nuclear Waste Policy Act of 1982, as amended, or any comparable successor law.

Officers' Certificate shall mean a certificate signed by the President or any Vice President and by the Treasurer, any Assistant Treasurer, the Secretary or any Assistant Secretary of the Person with respect to which such term is used.

Original Loan Participants shall mean Bank of America and each of the other banks listed in Schedule 1 to the Participation Agreement.

Operating Agent shall have the meaning assigned thereto in the ANPP Participation Agreement.

Outstanding when used with respect to the Notes, shall mean, as of the date of determination, all such Notes theretofore issued, authenticated and delivered under the Indenture, except (a) Notes theretofore cancelled by the Indenture Trustee or delivered to the Indenture Trustee for cancellation, (b) Notes or portions thereof for the payment of which the Indenture Trustee holds (and has notified the Holders thereof that it holds) in trust for that purpose an amount sufficient to make full payment thereof when due, (c) Notes or portions thereof which have been pledged as collateral for any obligations of the obligor thereof to the extent that an amount sufficient to make full payment of such obligations when due has been deposited with the pledgee of such Notes for the purpose of holding such amount in trust for the payment of such obligations in accordance with the indenture or agreement under which such obligations are secured and (d) Notes in exchange for, or in lieu of, which other Notes have been issued, authenticated and delivered pursuant to the Indenture; provided, however, that any Note owned by the Lessee, the Equity Participant or the Owner Trustee or any Affiliate of either thereof shall be disregarded and deemed not to be Outstanding for the purpose of any Directive.

Overdue Interest Rate shall mean the weighted average rate per annum of interest payable with respect to overdue payments of principal on the Notes Outstanding, computed as set forth in such Notes.

Owner Trustee shall mean The First National Bank of Boston, a national banking association, not in its individual capacity, but solely as Owner Trustee under the Trust Agreement, and each successor as trustee, separate trustee and co-trustee thereunder.

Participation Agreement shall mean the Participation Agreement, dated as of August 1, 1986, among the Owner Trustee, the Indenture Trustee, the Agent, Funding Corp, the Equity Participant and APS.

Penalty Rate shall mean the higher of (x) 2% per annum in excess of the Prime Rate and (y) 1% in excess of the Overdue Rate.

Period shall mean the length of time for which an action or event is stated or otherwise known at its inception to be in existence (determined by the terms of such action or event or the surrounding circumstances), or is expected at its inception to be in existence as determined by an independent nuclear engineering consultant or firm having expertise in the area of nuclear electric generating plants designated by Lessor and Lessee within 10 days after either shall request such designation (which Lessor or Lessee may do at any time after such action or event occurs) or, if Lessor and Lessee are unable to agree on such consultant or firm within such 10-day period, designated by the American Arbitration Association, or any organization successor thereto, within 7 days after either Lessor or Lessee shall request such organization so to do (which Lessor or Lessee may do at any time after the expiration of such 10-day period). Such consultant or firm shall render its determination within 14 days after its designation, which determination shall be final, binding and conclusive on Lessor and Lessee. The fees and expenses of such consultant or firm shall be shared equally by Lessor and Lessee.

Permitted Liens shall mean (i) the respective rights and interests of the Lessee, the Equity Participant, the Lessor, the Loan Participant and the Indenture Trustee, as provided in the Transaction Documents; (ii) the rights of any sublessee or assignee under a sublease or an assignment permitted by the terms of the Facility Lease; (iii) the Lien of the Existing Mortgage on the leasehold estate under the Facility Lease; (iv) Liens for taxes on the Undivided Interest or the PVNGS Site either not yet due or which are being contested in good faith and by appropriate proceedings diligently conducted, so long as such proceedings shall not (x) involve any danger of the sale, forfeiture or loss of the Undivided Interest, any part thereof or interest therein, (y) interfere with the use, possession or disposition of the Undivided Interest, or any part

thereof or interest therein, or (z) impair payment of Rent; (v) inchoate materialmen's, mechanics', workmen's, repairmen's, employees', carriers', warehousemen's, or other like Liens arising in the ordinary course of business for PVNGS, and not delinquent; (vi) Lessor's Liens, Equity Participant's Liens and Indenture Trustee's Liens; (vii) choate Liens that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor shall have been made and which are being contested diligently by the appropriate party in good faith and by appropriate proceedings so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (viii) choate Liens of any of the types described in clause (v) above that have been bonded for the full amount in dispute or as to which other security arrangements satisfactory to the Lessor and the Equity Participant shall have been made and which arise out of judgments or awards and with respect to which (A) an appeal or proceeding for review is being prosecuted in good faith and for the payment of which adequate reserves shall have been provided as required by good accounting practice and (B) there shall have been secured a stay of execution pending such appeal or proceeding for review, so long as such proceedings shall not violate clause (x), (y) or (z) of clause (iv) above; (ix) the rights and interests of the Lessee under the Assignment and Assumption; (x) the rights of the NRC under the License; (xi) the rights of the ANPP Participants (other than (i) the Lessee and (ii) any Person who shall become an ANPP Participant in respect of the Undivided Interest under the ANPP Participation Agreement or any other ANPP Project Agreement; and (xii) Liens on the undivided ownership interests in Unit 2 owned by ANPP Participants and other Persons (other than the Lessee).

Person shall mean any individual, partnership, corporation, trust, unincorporated association or joint venture, government or any department or agency thereof, or any other entity.

PNM shall mean Public Service Company of New Mexico, a New Mexico corporation.

Price-Anderson Act shall mean the Price-Anderson Act, Pub. L. No. 85-256, 71 Stat. 576 (1957), as amended to August 18, 1986, including amendments to Section 170 of the Atomic Energy Act and to any definition relevant to said Section 170.

Pricing Assumptions shall mean the pricing assumptions set forth in Schedule 2 to the Participation Agreement.

Prime Rate shall mean the rate of interest publicly announced from time to time by Chemical Bank at its principal office in New York City as its prime or base lending rate. Any change in the Prime Rate shall be effective on the date such change in the Prime Rate is announced.

Project Insurance shall have the meaning assigned thereto in the ANPP Participation Agreement.

Project Manager shall have the meaning assigned thereto in the ANPP Participation Agreement.

Prudent Utility Practice shall mean, at a particular time, any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry prior to such time, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at the lowest reasonable cost consistent with good business practices, reliability, safety and expedition. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act to the exclusion of all others, but rather to a spectrum of possible practices, methods or acts having due regard for, among other things, manufacturers' warranties and the requirements of governmental agencies of competent jurisdiction and the requirements of the Transaction Documents.

Purchase Documents shall mean the Bill of Sale, the Deed and such other documents as the Equity Participant, the Owner Trustee, the Indenture Trustee, the Loan Participant or their respective counsel shall deem desirable to convey good and marketable title to the Undivided Interest and the Real Property Interest to the Trust.

Purchase Price shall have the meaning set forth in Section 4(a) of the Participation Agreement.

PVNGS shall mean the Arizona Nuclear Power Project, as that term is defined in the ANPP Participation Agreement.

PVNGS Site shall mean the interest in Title USA Trust No. 530 and the real property described in Exhibit A to the Bill of Sale.

Real Estate Investment shall have the meaning set forth in Section 3(a) of the Participation Agreement.

Real Property Interest shall mean the interest of the Lessor in the PVNGS Site (excluding Title USA Trust No. 530) created by the Deed.

Reasonable Basis for a position shall exist if tax counsel may properly advise reporting such position on a tax return in accordance with Formal Opinion 85-352 issued by the Standing Committee on Ethics and Professional Responsibility of the American Bar Association.

Refunding Amount shall mean the amount required to fund Funding Corp's Refunding Loan.

Refunding Bonds shall mean any series of bonds of Funding Corp issued, authenticated and delivered under the Collateral Trust Indenture, as supplemented by a Refunding Supplemental Indenture, the proceeds of which will be used to refund Outstanding Notes.

Refunding Date shall mean any date of issuance of Refunding Notes.

Refunding Loan shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Refunding Notes shall have the meaning set forth in Section 2(e) of the Participation Agreement.

Refunding Supplemental Indenture shall mean the Refunding Bond Supplemental Indenture among APS, Funding Corp and the Collateral Trust Trustee, supplementing the Collateral Trust Indenture and providing, among other things, for the issuance of the Refunding Bonds.

Registration Statement shall mean the registration statement on Form S-3, including all exhibits and all documents incorporated in the Registration Statement by reference, to be filed with the SEC under the Securities Act in connection with the offer, issue and sale of the Refunding Bonds.

Regulations shall mean the income tax regulations issued, published or promulgated under the Code.

Releveraging Amount shall mean that portion of the initial principal amount of the Refunding Notes in excess of the unpaid principal amount of the Outstanding Notes being refunded.

Releveraging Loan shall have the meaning set forth in Section 2(c) of the Participation Agreement.

Renewal Option shall mean the option to elect an extension of the Facility Lease for either the Fixed Rate Renewal Term or the Fair Market Renewal Term.

Renewal Term shall have the meaning set forth in Section 12 of the Facility Lease.

Rent shall mean Basic Rent and Supplemental Rent.

Rent Differential shall have the meaning set forth in Section 3(h) of the Facility Lease.

Requisition of Title shall mean any circumstance or event in consequence of which Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be condemned or seized or title thereto shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Requisition of Use shall mean any circumstance or event other than a Requisition of Title in consequence of which the use of Unit 2 or the Undivided Interest (or all or any portion of the Real Property Interest, the loss of which would significantly interfere with the use of Unit 2 or the Undivided Interest) shall be requisitioned or taken by any Governmental Authority under power of eminent domain or otherwise.

Responsible Officer shall mean, with respect to the subject matter of any covenant, agreement or obligation of any party contained in any Transaction Document, the President, any Vice President, Assistant Vice President, Treasurer, Assistant Treasurer or other officer who in the normal performance of his operational responsibility would have knowledge of such matter and the requirements with respect thereto.

Retained Assets shall mean (i) the Lessee's interest in PVNGS other than the Undivided Interest and the Real Property Interest, (ii) Severable Capital Improvements title to an undivided interest in which is retained by the Lessee in accordance with Section 8(e) of the Facility Lease, and (iii) any additional interest in and to PVNGS (other than the Undivided Interest and the Real Property Interest) to which the Lessee becomes entitled in consequence of Sections 16.2 or 23.5 of the ANPP Participation Agreement (except as otherwise provided in Section 5(a) or 19 of the Facility Lease).

Sale Proceeds shall mean, with respect to any sale of the Undivided Interest and the Real Property Interest by the Lessor to any Person, the gross proceeds of such sale paid in cash, less all costs and expenses whatsoever incurred by the Lessor and the Equity Participant in connection therewith.

Salt River shall mean Salt River Project Agricultural Improvement and Power District, an Arizona agricultural improvement district.

SCPPA shall mean Southern California Public Power Authority, a California joint powers agency (doing business in Arizona as Southern California Public Power Authority Association).

SEC shall mean the Securities and Exchange Commission of the United States of America, or any successor agency.

Section 6(c) Application shall mean Funding Corp's Application for an Order under Section 6(c) of the Investment Company Act of 1940 Exempting PVNGS Funding Corp., Inc. from All Provisions of such Act, as filed with the SEC on May 13, 1986, as amended.

Section 48(d) Election shall have the meaning set forth in Section 19(i)(1) of the Participation Agreement..

Securities Act shall mean the Securities Act of 1933, as amended.

Securities Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

Severable, when used with respect to any Capital Improvement, shall mean any Capital Improvement which can be readily removed from Unit 2 without materially damaging Unit 2 or materially diminishing or impairing the value, utility or condition of Unit 2.

Southern California shall mean Southern California Edison Company, a California corporation.

Special Casualty Value, as of any date, shall mean (i) during the Basic Lease Term, the percentage of Facility Cost set forth opposite such date in Schedule 3 to the Facility Lease, and (ii) during any Renewal Term, the amount determined by amortizing ratably the present value of Basic Rent (discounted at a rate of 10%) payable in respect of the Undivided Interest for such Renewal Term (retaining a residual of the anticipated Fair Market Sales Value of the Undivided Interest as of the last day of such Renewal Term) in semi-annual steps over the period from such date to the License Expiration Date. Anything contained in the Participation Agreement or the Facility Lease to the contrary notwithstanding, Special Casualty Value shall be, when added to all other amounts which the Lessee is required to pay under Section 9(d) of the Facility Lease, under any circumstances and in any event, in an amount at least sufficient to pay in full, as of any date of payment, the aggregate unpaid principal amount of all Notes Outstanding at the close of business on such date, together with accrued and unpaid interest on such Notes.

Special Transfer shall have the meaning set forth in Section 7(b)(4) of the Participation Agreement.

Standard & Poors shall mean Standard & Poors Corporation and any successor issuing nationally accepted security ratings.

Summary Statement shall have the meaning set forth in Section 19(i) of the Participation Agreement.

Substituted Lessee shall have the meaning set forth in Section 6.8(b) of the Indenture.

Supplemental Financing shall mean a financing of the Supplemental Financing Amount of Capital Improvements made pursuant to Section 8(f) of the Facility Lease.

Supplemental Financing Amount shall mean that portion of the cost of a Capital Improvement to Unit 2 which equals (i) the amount of the increase, if any, in the Equity Participant's basis in the Undivided Interest for purposes of section 1012 or 1016 of the Code as a result of such Capital Improvement less (ii) the amount of any related Additional Equity Investment of the Lessor.

Supplemental Rent shall have the meaning set forth in Section 3(b) of the Facility Lease.

Surviving Lessee shall have the meaning set forth in Section 10(b)(3)(ii)(A) of the Participation Agreement.

Taxes shall mean any and all fees (including, without limitation, documentation, recording, license and registration fees), taxes (including, without limitation, net income, franchise, value added, ad valorem, excise, gross income, gross receipts, sales, use, property, (personal or real, tangible or intangible), and stamp taxes), levies, imposts, duties, charges, assessments, or withholdings of any nature whatsoever, general or special, ordinary or extraordinary, together with any and all penalties, fines, additions to tax and interest thereon..

Tax Assumptions shall mean the assumptions set forth in Section 1(a) of the Tax Indemnification Agreement with respect to the Federal income tax consequences of the transactions contemplated by the Transaction Documents.

Tax Indemnification Agreement shall mean the Tax Indemnification Agreement, dated as of August 1, 1986, between APS and the Equity Participant.

Termination Date shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Event shall mean any early termination of the Facility Lease in accordance with Section 14 thereof.

Termination Notice shall have the meaning set forth in Section 14(a) of the Facility Lease.

Termination Obligation shall have the meaning set forth in Section 15.10.2 of the ANPP Participation Agreement (or any comparable successor provision).

Transaction Documents shall mean the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents and the Notes.

Transaction Expenses shall have the meaning set forth in Section 14(a) of the Participation Agreement.

Transfer shall mean the transfer, by bill of sale or otherwise, by the Lessor of all the Lessor's right, title and interest in and to the Undivided Interest, the Real Property Interest and the Assignment and Assumption on an "as is, where is" basis, free and clear of all Lessor's Liens and Equity Participant's Liens (but subject to the lien of the Indenture if and to the extent it attaches), but otherwise without recourse, representation or warranty (including an express disclaimer of representations and warranties in a manner comparable to that set forth in the second sentence of Section 6(b) of the Facility Lease), together with the due assumption by the transferee of, and the due release of the Lessor from, all of the Lessor's obligations under the Assignment and Assumption and the Deed by an instrument or instruments satisfactory in form and substance to the Lessor and the Equity Participant.

Transferee shall have the meaning set forth in Section 15 of the Participation Agreement.

Trust shall mean the trust created by the Trust Agreement.

Trust Agreement shall mean the Trust Agreement, dated as of August 1, 1986, between Emerson Finance Co. and FNB.

Trust Estate shall have the meaning set forth in Section 2.03 of the Trust Agreement.

Trust Indenture Act shall mean the Trust Indenture Act of 1939, as amended.

Trustee's Expenses shall mean any and all liabilities, obligations, costs, compensation, fees, expenses and disbursements (including, without limitation, legal fees and expenses) of any kind and nature whatsoever (other than such amounts as are included in Transaction Expenses) which may be imposed on, incurred by or asserted against the Indenture Trustee or any of its agents, servants or representatives, in any way relating to or arising out of the Indenture, the Lease Indenture Estate, the Participation Agreement or the Facility Lease, or any document contemplated thereby, or the performance or enforcement of any of the terms thereof, or in any way relating to or arising out of the administration of the Lease Indenture Estate or the action or inaction of the Indenture Trustee under the Indenture; provided, however, that such amounts shall not include any Taxes or any amount expressly excluded from the Lessee's indemnity obligations pursuant to Section 13(a) or 13(b) of the Participation Agreement.

UCC or Uniform Commercial Code shall mean the Uniform Commercial Code as in effect in any applicable jurisdiction.

Underwriting Agreement shall mean an agreement among Funding Corp., APS, and the underwriter or underwriters for any Refunding Bonds relating to the purchase, sale and delivery of such Refunding Bonds.

Undivided Interest shall mean the Lessor's undivided interest in Unit 2 (other than Unit 2 Retained Assets), including, except where expressly stated to the contrary, the related Generation Entitlement Share attributable thereto.

Uniform System of Accounts shall mean the Uniform System of Accounts prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act (Class A and Class B), 18 CFR 101, as in effect on the date of execution of the Participation Agreement, as amended or modified from time to time after such date.

Unit 2 shall mean the 1,270 megawatt unit, commonly known as Unit 2, at the Palo Verde Nuclear Generating Station, all as more fully described in Exhibit B to the Bill of Sale, together with all Capital Improvements thereto.

Unit 2 Interest shall mean a percentage equal to the Owner Trustee's undivided interest in all of Unit 2, the percentage of which is set forth in Schedule 3 to the Participation Agreement.

Unit 2 Retained Assets shall mean (1) all resident fuel assemblies, equipment and personal property constituting part of the Generating Unit (as defined in the ANPP Participation Agreement) designated as Palo Verde Nuclear Generating Station Unit 2 (other than the common facilities) owned by the Lessee but excluded from Unit 2 as set forth in Exhibit B to the Bill of Sale, (2) a one-third interest in all equipment and personal and real property constituting PVNGS common facilities under the ANPP Participation Agreement owned by the Lessee, including but not limited to (i) surveillance systems, including associated radioactive monitoring systems and equipment; (ii) water treatment facilities and transport systems for supply of waste water effluent; (iii) warehouses and related storage facilities and equipment; (iv) nuclear fuel, including spare fuel assemblies; (v) all transmission and ANPP High Voltage Switchyard facilities; (vi) administration building; (vii) administration annex building; (viii) technical support center; (ix) visitor center; (x) external communication systems and equipment, including associated interconnections and computer data links; (xi) parking lot improvements, road improvements, fencing and dikes; (xii) spare parts (common

facilities); (xiii) simulator; and (xiv) oil and diesel fuel inventories, (3) all real property, leases, licenses, easements, rights-of-way and other property held by Title USA Company of Arizona Trust 530 established by that certain Trust Agreement dated October 15, 1975, as amended, but excluding therefrom all improvements, and (4) those ANPP Project Agreements (as defined in the ANPP Participation Agreement), in addition to the Trust Agreement for Title USA Company of Arizona Trust 530, consisting of leases, licenses, easements, and permits, which provide land and land rights for (i) the pipeline to supply waste water effluent to PVNGS from the 91st Avenue sewage treatment plant serving the Phoenix metropolitan area and (ii) railroad access to the Nuclear Plant Site (as defined in the ANPP Participation Agreement).

Unit 2 Retained Assets Portion shall mean the percentage set forth on Schedule 3 to the Participation Agreement.

User shall mean a Person unrelated to APS (within the meaning of Section 318 of the Code) possessing the Undivided Interest after the Lease Termination Date.

COLLATERAL TRUST INDENTURE

dated as of November 1, 1986

AMONG

PVNGS FUNDING CORP., INC.,

ARIZONA PUBLIC SERVICE COMPANY

AND

CHEMICAL BANK,
as Trustee

**Providing for the Issuance from Time to Time of
Securities To Be Issued in One or More Series**

PALO VERDE NUCLEAR GENERATING STATION

PVNGS FUNDING CORP., INC.
ARIZONA PUBLIC SERVICE COMPANY

Reconciliation and tie between Indenture
dated as of , 1986

and

Trust Indenture Act of 1939

<u>Section of Act</u>	<u>Section of Indenture</u>
310(a) (1)	9.09
(2)	9.09
(3)	Inapplicable
(4)	Inapplicable
(b)	9.08, 9.10(a), 9.10(d), 9.10(e), 9.11
(c)	Inapplicable
311(a) (b)	9.13
(c)	Inapplicable
312(a)	10.01
(b)	10.02(a)
(c)	10.02(b)
(c)	10.02(c)
313(a)	10.03(a)
313(b) (1)	10.03(b) (1)
(2)	10.03(b)
(c)	10.03(a) & (b)
(d)	10.03(c)
314(a)	10.04
(b)	5.06
(c) (1)	1.02
(2)	1.02
(3)	2.04(7) (A)
(d) (1)	5.11, 5.12
(2)	Inapplicable
(3)	2.04(7) (B)
(e)	1.02
315(a) (1)	9.01(a) (1)
(2)	9.01(a) (2)
315(a) (last clause)	9.01(a) (2)
(b)	9.02
(c)	9.01(b)
(d) (1)	9.01(c) (1)

<u>Section of Act</u>	<u>Section of Indenture</u>
(2)	9.01(c) (2)
(3)	9.01(c) (3)
(e)	8.10
316(a) (1) (A)	8.07
(B)	8.08
(2)	Inapplicable
(a) (last sentence)	1.01 ("Outstanding")
(b)	8.11
317(a) (1)	8.05(a)
(2)	8.05(d)
(b)	5.03
(c) (2)	9.14
318(a)	1.07

NOTE: This reconciliation and tie shall not, for any purpose, be deemed to constitute a part of the Indenture.

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COLLATERAL TRUST INDENTURE, dated as of November 1, 1986, among PVNGS FUNDING CORP., INC., a Delaware corporation (hereinafter called the *Company*), having its principal office and mailing address at Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 19801, ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, having its principal office and mailing address at 411 North Central Avenue, Phoenix, Arizona 85072-3999 (hereinafter called *APS*), and CHEMICAL BANK, a New York banking corporation, as Trustee (hereinafter called the *Trustee*), having its corporate trust office at 55 Water Street, New York, New York 10041.

RECITALS

WHEREAS, the Company has duly authorized the creation of an issue of its debentures, notes or other evidences of indebtedness to be issued in one or more series (the *Securities*) up to such principal amount or amounts as may from time to time be authorized in accordance with the terms of this Indenture; and to secure the Securities and to provide for the authentication and delivery thereof by the Trustee, the Company has duly authorized the execution and delivery of this Indenture; and

WHEREAS, all acts necessary to make this Indenture a valid instrument for the security of the Securities, in accordance with its and their terms, have been done;

NOW, THEREFORE, THIS INDENTURE WITNESSETH, that, to secure the payment of the principal of, and premium (if any) and interest on, all the Securities authenticated and delivered hereunder and issued by the Company and outstanding, and the performance of the covenants therein and herein contained, and in consideration of the premises and of the covenants herein contained and of the purchase of the Securities by the holders thereof, and of the sum of one dollar (\$1.00) paid to the Company by the Trustee at or before the delivery hereof, the receipt whereof is hereby acknowledged, the Company by these presents does grant, bargain, sell, release, convey, assign, pledge, transfer, mortgage, hypothecate, and confirm unto the Trustee all and singular the following (which collectively are hereinafter called the *Pledged Property*), excluding, in any event, any moneys which are specifically stated herein not to constitute part of the Pledged Property, to wit:

CLAUSE FIRST

All Pledged Lessor Notes (as hereinafter defined) as shall be actually pledged and assigned by the Company to the Trustee pursuant to the Series Supplemental Indentures or other supplemental indentures to be executed and delivered as provided in this Indenture, together with the interest of the Company (if any) in the Lease Indentures (as hereinafter defined) securing said Pledged Lessor Notes.

CLAUSE SECOND

All right, title and interest of the Company in, to and under any agreements with respect to commitment fees or other amounts payable by APS entered into between APS and the Company in connection with the issuance and sale of any series of Securities, if actually assigned by the Company to the Trustee pursuant to a Series Supplemental Indenture or other supplemental indentures to be executed and delivered as provided in this Indenture.

CLAUSE THIRD

All the proceeds received by the Company from the sale of the Securities, all the tolls, rents, issues, profits, products, revenues and other income of the property subjected or required to be subjected to the lien of this Indenture, and all the estate, right, title and interest of every nature whatsoever of the Company in and to the same and every part thereof.

CLAUSE FOURTH

Any property, including cash, that may, from time to time hereafter be subjected to the lien and/or pledge hereof by the Company or which pursuant to any provision of this Indenture or any Series Supplemental Indenture or other supplemental indentures to be executed and delivered as provided in this Indenture may become subjected to the lien and/or pledge hereof; and the Trustee is hereby authorized to receive the same at any time as additional security hereunder. Such subjection to the lien hereof of any such property as additional security may be made subject to any reservations, limitations or conditions which shall be set forth in a written instrument executed by the Company and/or by the Trustee respecting the scope or priority of such lien and/or pledge or the use and disposition of such property or the proceeds thereof.

TO HAVE AND TO HOLD the Pledged Property unto the Trustee and its successors and assigns forever subject to the terms of this Indenture, including, without limitation, Section 12.01.

BUT IN TRUST, NEVERTHELESS, for the equal and proportionate benefit and security of the holders from time to time of all the Securities authenticated and delivered hereunder and issued by the Company and outstanding, without any priority of any one Security over any other.

AND UPON THE TRUSTS and subject to the covenants and conditions hereinafter set forth.

ARTICLE ONE

DEFINITIONS AND OTHER PROVISIONS OF GENERAL APPLICATION.

SECTION 1.01. *Definitions.*

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

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

(2) all other terms used herein which are defined in the Trust Indenture Act (as hereinafter defined), either directly or by reference therein, have the meanings assigned to them therein;

(3) all accounting terms not otherwise defined herein have the meanings assigned to them in accordance with generally accepted accounting principles;

(4) all reference in this Indenture to designated "Articles", "Sections" and other subdivisions are to the designated Articles, Sections and other subdivisions of this Indenture; and

(5) 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.

Certain terms, used principally in Article Nine, are defined in that Article.

"Act" when used with respect to any Holder has the meaning specified in Section 1.04.

"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.

"APS" means Arizona Public Service Company, an Arizona corporation, and, subject to the provisions hereof, its successors and assigns.

"Authorized Agent" means any Paying Agent or Security Registrar or other agent appointed by the Trustee in accordance with this Indenture to perform any function which this Indenture authorizes the Trustee or such agent to perform.

"Board of Directors" means the board of directors of the Company, when used with respect to the Company, and either the board of directors, or any committee of that board duly authorized to act for it hereunder, when used with respect to APS.

"Board Resolution" means a copy of a resolution certified by the Secretary, an Assistant Secretary or an Associate Secretary of the Company or APS, as the case may be, to have been duly adopted by the Board of Directors of such entity and to be in full force and effect on the date of such certification, and delivered to the Trustee.

"Business Day" means any day other than a Saturday or Sunday or other day on which banks in Phoenix, Arizona, New York, New York or Boston, Massachusetts are authorized or obligated to be closed.

"Change" with respect to any instrument means any consent, amendment, waiver, approval, notice or direction or the execution, grant or giving of any thereof.

"Commission" means the Securities and Exchange Commission, as from time to time constituted, created under the Securities Exchange Act of 1934, 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 on such date.

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

"Company Request" and *"Company Order"* mean, respectively, a written request or order signed in the name of the Company by its President or one of its Vice Presidents, and by its Treasurer, Secretary, or one of its Assistant Treasurers or Assistant Secretaries or Associate Secretaries, and delivered to the Trustee.

"Corporate Trust Office" means the principal office of the Trustee at which at any particular time corporate trust business of the Trustee shall be administered, which at the date of this Indenture is 55 Water Street, New York, N.Y. 10041, Attention: Corporate Trustee Administration.

"Equity Participant" means any Equity Participant identified in a Schedule to a Series Supplemental Indenture, until a successor or assignees thereof shall have become such pursuant to the applicable provisions of the Participation Agreement to which such Equity Participant is a party, and thereafter *"Equity Participant"* means such successor or assignees; *"Equity Participants"* means each and every Equity Participant.

"Event of Default" has the meaning specified in Section 8.01.

"Extension Letter" means the Extension Letter, to be dated the date of issue of a Pledged Lessor Note and addressed to the Trustee by the parties to the Participation Agreement pursuant to which such Pledged Lessor Note was issued, extending to the Trustee the representations, warranties and covenants of such parties set forth in such Participation Agreement.

"Holder" or *"Securityholder"* means a Person in whose name a Security is registered in the Security Register.

"Indenture" means this instrument as originally executed and as it may from time to time be supplemented or amended by one or more indentures supplemental hereto entered into pursuant to the applicable provisions hereof.

"Initial Interest Date" with respect to any series of Securities means the date of the Stated Maturity for the initial installment of interest on Securities of such series.

"Lease" means any Lease identified in a Schedule to a Series Supplemental Indenture, as such Lease may be amended from time to time pursuant to the applicable provisions thereof; *"Leases"* means each and every Lease.

"Lease Indenture" means any Lease Indenture identified in a Schedule to a Series Supplemental Indenture, as such Lease Indenture may be amended or supplemented from time to time pursuant to the applicable provisions thereof; *"Lease Indentures"* means each and every Lease Indenture.

"Lease Indenture Trustee" means the Lease Indenture Trustee identified in a Schedule to a Series Supplemental Indenture, until a successor Lease Indenture Trustee shall have become such pursuant to the applicable provisions of the Lease Indenture to which such Lease Indenture Trustee is a party, and thereafter *"Lease Indenture Trustee"* means the successor Lease Indenture Trustee; *"Lease Indenture Trustees"* means each and every Lease Indenture Trustee.

"Lease Payments" with respect to any Lease shall mean amounts payable under such lease in respect of (i) interim rent (if any), (ii) basic rent, (iii) casualty value, (iv) special casualty value, (v) extraordinary casualty value or (vi) any other amounts payable in connection with termination of such Lease, in each case as more fully described in and assigned pursuant to the related Lease Indenture; *"Lease Payments"* with respect to all Leases means the aggregate of Lease Payments under any and all Leases.

"Lessee Request" and *"Lessee Order"* mean, respectively, a written request and a written order signed in the name of APS by its President or one of its Vice Presidents or Assistant Vice Presidents and by its Treasurer or Secretary or one of its Assistant Treasurers or Assistant Secretaries or Associate Secretaries, or by any authorized agent of APS, and delivered to the Trustee.

"Lessor" or *"Owner Trustee"* means any Lessor or Owner Trustee identified in a Schedule to a Series Supplemental Indenture, until a successor shall have become such pursuant to the applicable provisions of the related Trust Agreement identified in said Schedule, and thereafter *"Lessor"* or *"Owner Trustee"* means such successor; *"Lessors"* or *"Owner Trustees"* means each and every Lessor or Owner Trustee.

"Lessor Note" means any promissory note issued by a Lessor under a Lease Indenture.

"Lien of this Indenture" or *"lien hereof"* means the lien and security interest created by these presents, or created by any concurrent or subsequent conveyance to the Trustee (whether made by the Company or any other Person and whether pursuant to a Series Supplemental Indenture or otherwise), or otherwise created, constituting any property a part of the Pledged Property held by the Trustee for the benefit of the Securities Outstanding hereunder.

"Obligor", when used with reference to the Securities or this Indenture, means APS and any successor to the obligations of APS under a Lease, and does not include the Trustee, the Lease Indenture Trustee, an Owner Trustee or an Equity Participant so long as they have not assumed such obligations; *provided, however*, that no reference to APS as an Obligor herein shall be construed as implying any guaranty by APS of the Securities.

"Officers' Certificate" means a certificate signed by the President or a Vice President, and by the Treasurer, the Secretary, or one of the Assistant Treasurers or Assistant Secretaries or Associate Secretaries, of APS, any Lessor or the Company, as the case may be, and delivered to the Trustee.

"Opinion of Counsel" means a written opinion of counsel for any Person either expressly referred to herein or otherwise satisfactory to the Trustee which may include, without limitation, counsel to the Company, any Lessor, the Lease Indenture Trustee, any Equity Participant or APS, whether or not such counsel is an employee of any of them.

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

(i) Securities theretofore cancelled by the Trustee or delivered to the Trustee for cancellation;

(ii) Securities for whose payment or redemption money in the necessary amount has been theretofore deposited with the Trustee in trust for the Holders of such Securities as provided in Section 12.01, provided that, if such Securities are to be redeemed (otherwise than through the operation of the Sinking Fund), notice of such redemption

has been duly given pursuant to this Indenture or provision therefor satisfactory to the Trustee has been made; and

(iii) Securities paid in full or in exchange for or in lieu of which other Securities have been authenticated and delivered pursuant to this Indenture unless held by a Holder in whose hands such Securities constitute valid obligations of the Company;

provided, however, that in determining whether the Holders of the requisite principal amount of Securities Outstanding have given any request, demand, authorization, direction, notice, consent or waiver hereunder, Securities owned by the Company or owned by APS or any Affiliate of the Company or of APS shall be disregarded and deemed not to be Outstanding, unless such Persons own 100% of the Securities owned by all Persons, except that, in determining whether the Trustee shall be protected in relying upon any such request, demand, authorization, direction, notice, consent or waiver, only Securities which the Trustee knows to be so owned shall be so disregarded. Securities so owned which have been pledged in good faith may be regarded as Outstanding if the pledgee establishes to the satisfaction of the Trustee the pledgee's right so to act with respect to such Securities and that the pledgee is not the Company or APS, or any Affiliate of the Company or of APS.

"*Participation Agreement*" means any Participation Agreement or other similar Lessor Note purchase document to which the Company is a party identified in a Schedule to a Series Supplemental Indenture, as such Participation Agreement or other purchase document may be amended from time to time pursuant to the applicable provisions thereof; "*Participation Agreements*" means each and every Participation Agreement.

"*Paying Agent*" means any Person acting as Paying Agent hereunder pursuant to Section 9.14.

"*Paying Agent's Office*" shall mean that office of the Paying Agent designated in Section 5.02.

"*Permitted Investment*" means (i) direct obligations of the United States of America, or (ii) obligations fully guaranteed by the United States of America, or (iii) certificates of deposit issued by, or bankers' accept-

ances of, or time deposits with, any bank, trust company or national banking association incorporated or doing business under the laws of the United States of America or one of the States thereof (but not exceeding \$15,000,000 in principal amount of all certificates of deposit and time deposits at any given time for any one bank, trust company or national banking association) having a combined capital and surplus of at least \$300,000,000 (including the Trustee, any Lease Indenture Trustee, any Lessor and any Paying Agent if such conditions are met), or (iv) commercial paper of companies incorporated or doing business under the laws of the United States of America or one of the States thereof (but not exceeding \$15,000,000 in principal amount at any given time for any one company) and in each case having a rating assigned to such commercial paper by Standard & Poor's Corporation or Moody's Investors Service, Inc. (or, if neither such organization shall rate such commercial paper at any time, by any nationally recognized rating organization in the United States of America) equal to the highest rating assigned by such organization, or (v) repurchase agreements fully collateralized by an obligation of the type described in clause (i) or (iv) above, pursuant to which a bank, trust company or national banking association referred to in clause (iii) above or another financial institution having a net worth of at least \$200,000,000 is obligated to repurchase any such obligation not later than 90 days after the purchase of any such obligation.

"Person" means any individual, corporation, partnership, joint venture, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

"Place of Payment", when used with respect to the Securities of any series, means the office or agency maintained pursuant to Section 5.02 and such other place or places, if any, where the principal of (and premium, if any) and interest on the Securities of that series are payable as specified in the Series Supplemental Indenture setting forth the terms of the Securities of such series.

"Pledged Lessor Note" means any Lessor Note identified in a Schedule to a Series Supplemental Indenture, as such Lessor Note may be amended or supplemented from time to time pursuant to the applicable provisions thereof, of the related Lease Indenture and of this Indenture; *"Pledged Lessor Notes"* means each and every Pledged Lessor Note.

"Pledged Property" has the meaning set forth in the Granting Clauses.

"Predecessor Securities" 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 2.09 in lieu of a lost, destroyed or stolen Security shall be deemed to evidence the same debt as the lost, destroyed or stolen Security.

"Principal Instruments" means the Pledged Lessor Notes, the Lease Indentures, the Participation Agreements and the Leases.

"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 (inclusive of accrued interest) at which it is to be redeemed pursuant to this Indenture and the terms of such Security.

"Regular Record Date" for the Stated Maturity of any installment of interest means the 15th day (whether or not a Business Day) next preceding such Stated Maturity.

"Responsible Officer" when used with respect to the Trustee means any officer of the Trustee customarily performing corporate trust functions.

"Security Register" has the meaning specified in Section 2.08.

"Security Registrar" means any Person acting as Security Registrar hereunder pursuant to Section 9.14.

"Series Supplemental Indenture" means an indenture supplemental to this Indenture, for the purpose of specifying, in accordance with Article Two hereof, the form of the Securities of any series, and/or for the purpose of subjecting to the Lien of this Indenture the Pledged Lessor Notes related to such series; *"Series Supplemental Indentures"* means each and every Series Supplemental Indenture.

"Sinking Fund" has the meaning specified in Section 7.01.

"Special Record Date" for the payment of any defaulted interest means a date fixed by the Trustee pursuant to Section 2.10.

"Stated Maturity" when used with respect to any Security or any installment of interest thereon means the date specified in such Security as the fixed date on which the principal of such Security or such installment of interest is due and payable, except that when used with reference to a series of Securities which have maturities from their respective dates of issuance of one year or less, the Series Supplemental Indenture creating such series

may provide that the Stated Maturity of all Securities of such series shall be a stated date beyond such individual maturity dates.

"Trust Indenture Act" or "TIA" means the Trust Indenture Act of 1939 as in force at the date as of which this instrument was executed, except as provided in Section 11.06.

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

SECTION 1.02. *Compliance Certificates and Opinions.*

Upon any application or request by the Company, any Lessor or APS to the Trustee to take any action under any provision of this Indenture, the Company, such Lessor or APS, as the case may be, shall furnish to the Trustee an Officers' 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, *except* 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:

- (1) a statement that each individual signing such certificate or opinion has read such covenant or condition and the definitions herein relating thereto;
- (2) 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;
- (3) a statement that, in the opinion of each such individual, he has made such examination or investigation as is necessary to enable him to express an informed opinion as to whether or not such covenant or condition has been complied with; and
- (4) a statement as to whether, in the opinion of each such individual, such condition or covenant has been complied with.

SECTION 1.03. *Form of Documents Delivered to Trustee.*

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.

Any certificate or opinion of an officer of the Company, of any Lessor or of APS may be based, in so far as it relates to legal matters, upon a certificate or opinion of, or representations by, counsel, unless such officer knows that the certificate or opinion or representations with respect to the matters upon which his certificate or opinion is based are erroneous. Any such certificate or Opinion of Counsel may be based, in so far as it relates to factual matters, upon a certificate or opinion of, or representations by, an officer or officers of the Company, of any Lessor or of APS, as the case may be, stating that the information with respect to such factual matters is in the possession of the Company, such Lessor or APS, respectively, unless such counsel knows that the certificate or opinion or representations with respect to such matters are erroneous.

Any Opinion of Counsel stated to be based on the opinion of other counsel shall be accompanied by a copy of such other opinion.

Where any Person is required to make, give or execute two or more applications, requests, consents, certificates, statements, opinions or other instruments under this Indenture, they may, but need not, be consolidated and form one instrument.

SECTION 1.04. *Acts of Holders.*

(a) Any request, demand, authorization, direction, notice, consent, waiver or other action provided by this Indenture to be 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; and, except as herein otherwise expressly provided, such action shall become effective when such instrument or instruments are delivered to the Trustee and, where it is hereby expressly required, to the Company and to APS. Such instrument or instruments

(and the action embodied therein and evidenced thereby) are herein sometimes referred to as the "Act" of the Holders 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 Indenture and (subject to Section 9.01) conclusive in favor of the Trustee, the Company and APS, if made in the manner provided in this Section.

(b) The fact and date of the execution by any Person of any such instrument or writing may be proved by the certificate of any notary public or other officer of any jurisdiction authorized to take acknowledgments of deeds or administer oaths that the Person executing such instrument acknowledged to him the execution thereof, or by an affidavit of a witness to such execution sworn to before any such notary or other such officer and where such execution is by an officer of a corporation or association or a member of a partnership, on behalf of such corporation, association or partnership, 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 Trustee deems sufficient.

(c) The ownership of Securities shall be proved by the Security Register and the Trustee shall not be affected by notice to the contrary.

(d) Any request, demand, authorization, direction, notice, consent, waiver or other action by the Holder of any Security shall bind the Holder of every Security issued upon the transfer thereof or in exchange therefor or in lieu thereof, whether or not notation of such action is made upon such Security.

SECTION 1.05. *Notices, etc., to Trustee, APS and Company.*

Any request, demand, authorization, direction, notice, consent, 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,

(1) the Trustee by any Holder, by the Company, by APS or by an Authorized Agent shall be sufficient for every purpose hereunder if made, given, furnished or filed in writing to or with the Trustee at its Corporate Trust Office, or

(2) the Company by the Trustee, by any Holder, by APS or by an Authorized Agent shall be sufficient for every purpose hereunder if in writing and mailed, first-class postage prepaid, to the Company ad-

dressed to it at the address of its principal office specified in the first paragraph of this instrument or at any other address previously furnished in writing to the Trustee and APS by the Company for such purpose, or

(3) APS by the Trustee, by any Holder, by the Company or by an Authorized Agent shall be sufficient for every purpose hereunder if in writing and mailed, first-class postage prepaid, to APS addressed to it at the address of its principal office specified in the first paragraph of this instrument or at any other address previously furnished in writing to the Trustee and the Company by APS for such purpose.

SECTION 1.06. *Notices to Holders; Waiver.*

Where this Indenture provides for notice to Holders of any event, such notice shall be sufficiently given (unless otherwise herein expressly provided) if in writing and mailed, first-class postage prepaid, to each Holder, at his address 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. Where this Indenture provides for notice in any manner, such notice may be waived in writing by the Person entitled to receive such notice, either before or after the event, 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. 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, and any notice which is mailed in the manner herein provided shall be conclusively presumed to have been duly given.

SECTION 1.07. *Conflict with Trust Indenture Act.*

If any provision hereof limits, qualifies or conflicts with another provision hereof which is required to be included in this Indenture by any of the provisions of the TIA, such required provision shall control. Notwithstanding the foregoing, the provisions of the TIA contained in Sections 9.08, 9.13 and 10.03 shall not become operative under this Indenture until this Indenture shall have been qualified under the TIA.

SECTION 1.08. *Effect of Heading and Table of Contents.*

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

SECTION 1.09. *Successors and Assigns.*

All covenants, agreements, representations and warranties in this Indenture by the Trustee, APS and the Company shall bind and, to the extent permitted hereby, shall inure to the benefit of and be enforceable by their respective successors and assigns, whether so expressed or not.

SECTION 1.10. *Separability Clause.*

In case any provision in this Indenture or in the Securities 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 1.11. *Benefits of Indenture.*

Nothing in this Indenture or in the Securities, expressed or implied, shall give to any Person, other than the parties hereto and their successors hereunder, or the Holders of Securities as expressly provided herein, any benefit or any legal or equitable right, remedy or claim under this Indenture.

SECTION 1.12. *Governing Law.*

This Indenture and each Security are being executed and delivered in the State of New York, shall be deemed to be contracts made in such State and for all purposes shall be construed in accordance with and governed by the laws of the State of New York.

SECTION 1.13. *Legal Holidays.*

In any case where the Redemption Date or the Stated Maturity of any Security or of any installment of interest, or any date on which any defaulted interest is proposed to be paid, shall not be a Business Day, then (notwithstanding any other provision of this Indenture) payment of interest and/or principal (and premium, if any) need not be made on such date, but shall be made on the next succeeding Business Day with the same force and effect as if made on the Redemption Date or at the Stated Maturity, or

on the date on which the defaulted interest is proposed to be paid, and no interest in respect of such payment shall accrue for the period from and after such Redemption Date or Stated Maturity, or date for the payment of defaulted interest, as the case may be.

ARTICLE TWO

THE SECURITIES

SECTION 2.01. *Form of Security to Be Established by Series Supplemental Indenture.*

The Securities of each series shall be in the form (not inconsistent with this Indenture, including Section 2.05 hereof) as shall be established in one or more Series Supplemental Indentures.

SECTION 2.02. *Form of Trustee's Authentication.*

The Trustee's certificate of authentication on all Securities shall be in substantially the following form:

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

CHEMICAL BANK
as Trustee

By _____
Authorized Officer

SECTION 2.03. *Amount Unlimited; Issuable in Series; Limitations on Issuance.*

The aggregate principal amount of Securities which may be authenticated and delivered under this Indenture is unlimited. Securities may be issued hereunder up to the aggregate principal amount which may be authorized from time to time by the Board of Directors of the Company.

The terms of any series of Securities relative to payment of principal thereof, and premium (if any) and interest thereon, need not correspond exactly to the schedule for such payments under the related Pledged Lessor Notes.

The Securities may be issued in one or more series. There shall be established in one or more Series Supplemental Indentures, prior to the issuance of Securities of any series:

(1) the title of the Securities of the series (which shall distinguish the Securities of the series from all other Securities) and the form or forms of Securities of such series;

(2) any limit upon the aggregate principal amount of the Securities of such series that 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 2.07, 2.08, 2.09, 6.06 or 11.07);

(3) the date or dates on which the principal of the Securities of such series is payable;

(4) the rate or rates at which the Securities of such series shall bear interest, or the method by which such rate shall be determined, the date or dates from which such interest shall accrue, the interest payment dates on which such interest shall be payable and the record dates for the determination of Holders to whom interest is payable;

(5) the place or places where the principal of, and premium, if any and interest on, Securities of such series shall be payable (if other than as provided in Section 5.02);

(6) the price or prices at which, the period or periods within which and the terms and conditions upon which Securities of such series may be redeemed, in whole or in part, at the option of the Company, pursuant to any sinking fund or otherwise;

(7) the obligation, if any, of the Company to redeem, purchase or repay Securities of such series pursuant to any sinking fund or analogous provisions or at the option of a Holder thereof and the price or prices at which and the period or periods within which and the terms and conditions upon which Securities of the series shall be redeemed, purchased or repaid, in whole or in part, pursuant to such obligation;

(8) if other than denominations of \$1,000 and any multiple thereof, the denominations in which Securities of such series shall be issuable;

(9) any other terms of such series (which terms shall not be inconsistent with the provisions of this Indenture); and

(10) any trustees, authenticating or paying agents, warrant agents, transfer agents or registrars with respect to the Securities of such series;

provided, however, that, after giving effect to the issuance of a new series of the Securities and the subjection to the Lien of this Indenture of the related Pledged Lessor Notes, the average of the daily balance of Excess Funds for each fiscal year of the Company shall not exceed 10% of the average of the aggregate principal amount of Securities Outstanding on each day in such fiscal year. For purposes of the foregoing proviso, "Excess Funds" shall mean, for any day, amounts actually paid to the Trustee under the Pledged Lessor Notes in excess of amounts then due and payable in respect of Securities.

SECTION 2.04. *Authentication and Delivery of Securities.*

At any time and from time to time after the execution and delivery of this Indenture, the Company may deliver Securities of any series executed by the Company to the Trustee for authentication, together with a Company Order for the authentication and delivery of such Securities, and the Trustee shall thereupon authenticate and deliver such Securities in accordance with such Company Order, without any further action by the Company. No Security shall be secured by or 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, in the form provided for herein, executed by the Trustee by one of its Responsible Officers, and such certificate upon any Security shall be conclusive evidence, and the only evidence, that such Security has been duly authenticated and delivered hereunder. In authenticating such Securities and accepting the additional responsibilities under this Indenture in relation to such Securities, the Trustee shall be entitled to receive, and (subject to Section 9.01) shall be fully protected in relying upon:

(1) an executed Series Supplemental Indenture;

(2) an Officers' Certificate of the Company (a) certifying as to resolutions of the Board of Directors of the Company by or pursuant to which the terms of the Securities of such series were established, (b) certifying that all conditions precedent under this Indenture to the Trustee's authentication and delivery of such Securities have been complied with and (c) certifying that (x) the terms of the documents

referred to in clauses (3) and (4) below are not inconsistent with the terms of this Indenture as then and theretofore supplemented and (y) such documents comply with Exhibit A hereto (if applicable);

(3) fully executed counterparts (but not the original thereof) of (a) the Lease Indentures under which were issued the Pledged Lessor Notes relating to such series of Securities and (b) the Leases relating to such Pledged Lessor Notes;

(4) the originals of the Pledged Lessor Notes relating to such series of Securities in an aggregate principal amount equal to not less than the aggregate principal amount of such series of Securities proposed to be authenticated and delivered;

(5) signed copies, either addressed to the Trustee or accompanied by statements that the Trustee may rely on such documents, of all certificates and opinions of counsel delivered (i) to the Company in connection with its purchase pursuant to the applicable Participation Agreements of the Pledged Lessor Notes relating to such series of Securities (ii) to the Lease Indenture Trustee in connection with the issuance of such Pledged Lessor Notes and (iii) to the Lessor under the applicable Lease or Participation Agreement in connection with any Refunding Loan, Releveraging Loan or Supplemental Financing (as such terms are defined in such Participation Agreement) and, to the extent not covered by such opinions, Opinions of Counsel (x) to the effect that: (a) the form or forms and the terms of such Securities have been established by a Series Supplemental Indenture as permitted by Sections 2.01 and 2.03 in conformity with the provisions of this Indenture; (b) such Securities, when authenticated and delivered by the Trustee and issued by the Company in the manner and subject to any conditions specified in such Opinion of Counsel, will constitute valid and binding obligations of the Company, except to the extent that the enforcement thereof may be limited by applicable bankruptcy, insolvency, reorganization, moratorium and other similar laws now or hereafter in effect relating to creditors' rights generally; and (c) all laws and requirements in respect of the execution and delivery by the Company of the Securities have been complied with; and (y) covering such other matters as the Trustee may reasonably request;

(6) duly executed Extension Letters relating to the Pledged Lessor Notes; and

(7) in circumstances where the Pledged Lessor Notes relating to such series of Securities are executed and delivered for the purposes described in clause (ii) of paragraph (1) of Section 3.5 of any Lease Indenture, (A) a certificate of an independent public accountant acceptable to the Trustee (who shall not be an employee of the Company, APS or any Affiliate of either) to the effect that the principal amount of Securities to be authenticated does not exceed the total cost (including allowance for funds used during construction to the extent permitted by generally accepted accounting principles) of any Capital Improvement (as defined in such Lease Indenture) financed with the proceeds of such Pledged Lessor Notes and (B) a certificate of an engineer, appraiser or other expert acceptable to the Trustee (who may be an officer or employee of APS except as would be required by Section 314(d)(3) of the Trust Indenture Act of 1939, as amended) to the effect that the fair value of any Capital Improvement as of its respective date of incorporation or installation was not less than the total cost (including allowance for funds used during construction to the extent permitted by generally accepted accounting principles) of such Capital Improvement as of the date financed with the proceeds of such Pledged Lessor Notes;

provided, however, that if a series of Securities is to be authenticated by the Trustee in advance of the actual delivery to the Trustee of the Pledged Lessor Notes relating thereto, (x) the documents described in the foregoing clauses (2)(c), (3), (4), (5) (other than the opinion described in subclauses (x) and (y)), (6) and (7) need not be delivered in connection with such authentication, but shall be delivered in connection with the release of the proceeds of the sale of such series of Securities in accordance with Sections 2.15 and 13.01 hereof and (y) the form of the Series Supplemental Indenture shall be appropriately modified to reflect the later delivery and pledge of the related Pledged Lessor Notes.

Receipt by the Trustee of the Officer's Certificate referred to in clause (2) above shall be conclusively presumed for all purposes of this Indenture to establish that the Lease Indentures, the Leases and the Pledged Lessor Notes referred to in such certification comply with the requirements of Exhibit A hereto.

The Trustee shall have the right to decline to authenticate and deliver any Securities under this Section if the Trustee, being advised by counsel, determines that such action may not lawfully be taken by the Company or if

the Trustee in good faith by its board of directors or board of trustees, executive committee, or a trust committee of directors or trustees and/or responsible officers shall determine that such action would expose the Trustee to personal liability.

SECTION 2.05. *Form and Denominations.*

The Securities of each series shall be in registered form and may have such letters, numbers or other marks of identification and such legends or endorsements printed, lithographed or engraved thereon, as may be required to comply with the rules of any securities exchange or to conform to any usage in respect thereof, or as may, consistently herewith, be prescribed by the Board of Directors of the Company or by the officers executing such Securities, such determination by said officers to be evidenced by their signing the Securities.

The definitive Securities shall be printed, lithographed or engraved or produced by any combination of these methods on steel engraved borders or may be produced in any other manner permitted by the rules of any securities exchange, all as determined by the officers executing such Securities, as evidenced by their execution of such Securities.

All Securities of any one series shall be substantially identical except as to denomination and Stated Maturity and except as may otherwise be provided herein or in the Series Supplemental Indenture setting forth the terms of the Securities of such series.

The Securities are issuable only in denominations of \$1,000 and/or any integral multiple thereof.

SECTION 2.06. *Execution of Securities.*

The Securities shall be executed on behalf of the Company by its President or one of its Vice Presidents under its corporate seal reproduced thereon and attested by its Secretary or one of its Assistant Secretaries. The signature of any such officers on the Securities may be manual or facsimile.

Securities bearing the manual or facsimile signatures of individuals who were at the time such signatures were affixed the proper officers of the Company shall bind the Company, notwithstanding that such individuals or any of them have ceased to hold such offices prior to the authentication and delivery of such Securities or did not hold such offices at the date of such Securities.

SECTION 2.07. *Temporary Securities.*

Pending the preparation of definitive Securities of any series, the Company may execute, and upon Company Order the Trustee shall authenticate and deliver, temporary Securities of such series which are printed, lithographed, typewritten, photocopied or otherwise produced, in any denomination, substantially of the tenor of the definitive Securities in lieu of which they are issued and 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.

If temporary Securities of any series are issued, the Company will cause definitive Securities of such series to be prepared without unreasonable delay. After the preparation of definitive Securities of such series, the temporary Securities of such series shall be exchangeable for definitive Securities of such series upon surrender of the temporary Securities of such series at the office or agency of the Company, for such purpose, in the Place of Payment, without charge to the Holder. Upon surrender for cancellation of any one or more temporary Securities of any series the Company shall execute and the Trustee shall authenticate and deliver in exchange therefor a like aggregate principal amount of definitive Securities of such series of authorized denominations. Until so exchanged such temporary Securities of any series shall in all respects be entitled to the same benefits under this Indenture as definitive Securities of such series.

SECTION 2.08. *Registration, Transfer and Exchange.*

The Trustee shall cause to be kept at the Corporate Trust Office a register in which, subject to such reasonable regulations as the Company may prescribe, the Company shall provide for the registration of Securities and of registration of transfers and exchanges of Securities. This register and, if there shall be more than one Security Registrar, the combined registers maintained by all such Security Registrars, are herein sometimes referred to as the "*Security Register*".

Upon surrender for registration of transfer of any Security of any series at the Corporate Trust Office, or at any office or agency maintained for such purpose pursuant to Section 9.14(a), 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 of the same Stated Maturity for principal and interest and of a like aggregate principal amount.

At the option of the Holders, Securities of any series may be exchanged for an equal aggregate principal amount of Securities of the same series and of the same Stated Maturity for principal and interest and of any authorized denominations, upon surrender of the Securities to be exchanged at the Corporate Trust Office, or at any office or agency maintained for such purpose pursuant to Section 9.14(a). Whenever any Securities are so surrendered for exchange, the Company shall execute, and the Trustee or a duly authorized authenticating agent shall authenticate and deliver, the Securities which the Securityholder making the exchange is entitled to receive.

All Securities issued upon any transfer or exchange of Securities shall be the valid obligations of the Company, evidencing the same debt, and entitled to the same security and benefits under this Indenture, as the Securities surrendered upon such transfer or exchange.

Every Security presented or surrendered for registration of transfer or exchange shall be duly endorsed, or be accompanied by a written instrument of transfer in form satisfactory to the Security Registrar duly executed, by the Holder thereof or his attorney duly authorized in writing.

No service charge shall be required of any Securityholders participating in any transfer or exchange of Securities in respect of such transfer or exchange, but the Security Registrar may require payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in connection with any transfer or exchange of Securities, other than exchanges pursuant to Sections 2.07, 6.06 or 11.07 not involving any transfer.

The Security Registrar shall not be required (i) to issue, transfer or exchange any Security of any series during a period beginning at the opening of business 15 days before the day of the mailing of a notice of redemption of Securities of such series selected for redemption under Section 6.02 or 7.02 and ending at the close of business on the day of such mailing, or (ii) to transfer or exchange any Security so selected for redemption in whole or in part except the unredeemed portion of any Security selected for redemption in part.

SECTION 2.09. *Mutilated, Destroyed, Lost and Stolen Securities.*

If (i) any mutilated Security is surrendered to the Trustee, or the Company, APS, the Security Registrar and the Trustee receive evidence to

their satisfaction of the destruction, loss or theft of any Security, and (ii) there is delivered to the Company, to APS, to the Security Registrar and to the Trustee evidence to their satisfaction of the ownership and authenticity thereof, and such security or indemnity as may be required by them to save each of them harmless, then, in the absence of notice to the Company, to APS, to the Security Registrar or to the Trustee that such Security has been acquired by a bona fide purchaser, the Company shall execute and upon its request the Trustee shall authenticate and deliver, in exchange for or in lieu of any such mutilated, destroyed, lost or stolen Security, a new Security of like tenor and principal amount, bearing a number not contemporaneously outstanding.

In case any such mutilated, destroyed, lost or stolen Security has become or is about to become due and payable, the Company may, upon satisfaction of the conditions set forth in clauses (i) and (ii) of the preceding paragraph, instead of issuing a new Security, pay such Security.

Upon the issuance of any new Security under this Section, the Security Registrar 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 expenses connected therewith.

Every new Security 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, and shall be entitled to all the security and benefits of this Indenture equally and proportionately with any and all other Securities 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 2.10. *Payment of Interest; Interest Rights Preserved.*

Interest on any Security which is payable, and is punctually paid or duly provided for, at any Stated Maturity of an installment of interest 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. At the option of the Company, payment of interest on any Security may be made by check mailed to the address of the Person entitled thereto as such address shall appear in the

Security Register or in such other manner as shall be established in a Series Supplemental Indenture creating the series of which such Security is a part.

Any interest on any Security of any series which is payable, but is not punctually paid or duly provided for, at any Stated Maturity of an installment of interest shall forthwith cease to be payable to the Holder on the relevant Regular Record Date by virtue of having been such Holder; and such defaulted interest may be paid by the Company, at its election in each case, as provided in paragraph (1) or paragraph (2) below:

(1) The Company may elect, which election shall be at the direction of any Lessor whose Pledged Lessor Note is in default in respect of the payment of interest and who is proposing to make payment of all or part of such defaulted interest, to make payment of any defaulted interest to the Persons in whose names the Securities of such series in respect of which interest is in default (or their respective Predecessor Securities) are registered at the close of business on a Special Record Date for the payment of such defaulted interest, which shall be fixed in the following manner. Such Lessor shall notify the Trustee and the Paying Agent in writing of the amount of defaulted interest proposed to be paid on each such Security and the date of the proposed payment, and at the same time there shall be deposited with the Trustee an amount of money equal to the aggregate amount proposed to be paid in respect of such defaulted interest or there shall be made 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 defaulted interest as in this paragraph provided. Thereupon the Trustee shall fix a Special Record Date for the payment of such defaulted interest which shall be not more than 15 nor less than 10 days prior to the date of the proposed payment and not less than 10 days after the receipt by the Trustee of the notice of the proposed payment. The Trustee shall promptly notify the Company, APS and the Security Registrar of such Special Record Date and, in the name and at the expense of the Company, shall cause notice of the proposed payment of such defaulted interest and the Special Record Date therefor to be mailed, first class postage prepaid, to each holder of a Security of such series at his address as it appears in the Security Register, not less than 10 days prior to such Special Record Date. Notice of the proposed payment of such defaulted interest and the Special Record Date therefor having been mailed as

aforesaid, such defaulted interest shall be paid to the Persons in whose names the Securities of such series (or their respective Predecessor Securities) are registered on such Special Record Date and shall no longer be payable pursuant to the following paragraph (2).

(2) The Company may make, or cause to be made, payment of any defaulted interest in any other lawful manner not inconsistent with the requirements of any securities exchange on which the Securities in respect of which interest is in default 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 paragraph, such payment shall be deemed practicable by the Trustee.

Subject to the foregoing provisions of this Section, each Security delivered under this Indenture upon 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, and each such Security shall bear interest from whatever date shall be necessary so that neither gain nor loss in interest shall result from such transfer, exchange or replacement.

SECTION 2.11. *Persons Deemed Owners.*

Prior to due presentment for registration of transfer, the Person in whose name any Security is registered shall be deemed to be the owner of such Security for the purpose of receiving payment of principal of (and premium, if any), and (subject to Section 2.10) interest on, such Security and for all other purposes whatsoever, whether or not such Security be overdue, regardless of any notice to anyone to the contrary.

SECTION 2.12. *Cancellation.*

All Securities surrendered for payment, redemption, credit against any Sinking Fund payment or redemption payment, transfer or exchange shall, if surrendered to any Person other than the Trustee, be delivered to the Trustee for cancellation. The Company may at any time deliver to the Trustee for cancellation any Securities previously authenticated and delivered hereunder which the Company may have acquired in any manner whatsoever, and all Securities so delivered shall be promptly cancelled by the Trustee. No Securities shall be authenticated in lieu of or in exchange for any Securities cancelled as provided in this Section, except as expressly

permitted by this Indenture. All cancelled Securities held by the Trustee shall be destroyed and certification of their destruction delivered to the Company unless, by Company Request, the Company otherwise directs.

SECTION 2.13. *Dating of Securities; Authentication.*

Except as otherwise provided in the Series Supplemental Indenture creating a series of Securities, each Security of any series shall be dated the date of the original issuance of the Securities of such series by the Company, which date shall be specified by the Company in the Company Order delivered to the Trustee pursuant to Section 2.04 in connection with the original authentication and delivery of the Securities of such series.

SECTION 2.14. *Source of Payments; Rights and Liabilities of Lessors and Equity Participants.*

Except as otherwise specifically provided in this Indenture, all payments of principal and premium (if any) and interest to be made by the Trustee in respect of the Securities or under this Indenture shall be made only from Pledged Property or the income and proceeds received by the Trustee therefrom. Each Holder, by its acceptance of a Security, agrees that (x) it will look solely to the Pledged Property or the income and proceeds received by the Trustee therefrom to the extent available for distribution to such Holder as herein provided and (y) none of any Equity Participant, any Lessor, any Lease Indenture Trustee or the Trustee is liable to any Holder or, in the case of any Equity Participant, Lessor and Lease Indenture Trustee, to the Trustee for any amounts payable under any Security or, except as provided herein with respect to the Trustee, for any liability under this Indenture. An Equity Participant, Lessor or Lease Indenture Trustee shall not have any duty or responsibility under this Indenture or the Securities to any Holder or to the Trustee.

SECTION 2.15. *Sale of Securities; and Application of Proceeds from the Sale of Securities.*

(a) Promptly upon receipt by the Company of the proceeds from any sale of a series of the Securities, the Company shall deposit such proceeds with the Trustee. The funds so deposited shall be held by the Trustee in a separate account as part of the Pledged Property and shall be invested, applied and distributed by the Trustee as provided herein.

(b) Subject to the provisions of Section 13.01, upon the issuance of the Pledged Lessor Notes related to any series of Securities and the delivery thereof to the Trustee to be subjected to the Lien of this Indenture pursuant to a Series Supplemental Indenture, the Trustee shall pay to the Lessor obligated in respect of any such Pledged Lessor Note, out of funds held by the Trustee in such separate account as Pledged Property, an amount equal to the principal amount of such Pledged Lessor Note in respect of which such Lessor is obligated. All payments to be made by the Trustee to any Lessor shall be made in immediately available funds at the respective offices designated by such Lessor.

ARTICLE THREE

PROVISIONS AS TO PLEDGED PROPERTY

SECTION 3.01. *Holding of Pledged Securities.*

The Trustee is authorized in its discretion to cause to be registered in its name, as Trustee, or in the name of its nominee, any and all coupon bonds which it may receive as part of the Pledged Property, or it may cause the same to be exchanged for registered bonds without coupons of any denomination. The Trustee may cause to be transferred into its name, as Trustee, or into the name of its nominee, any and all registered bonds which it may receive as part of the Pledged Property, or may cause such registered bonds to be exchanged for coupon bonds. All Pledged Lessor Notes assigned to and pledged with the Trustee pursuant to any provision of this Indenture or any Series Supplemental Indenture shall be endorsed in blank for transfer or be accompanied by proper instruments of assignment satisfactory to the Trustee, duly executed by the Company. The Company will deliver promptly to the Trustee such documents, certificates and opinions as the Trustee may reasonably request in connection with subjection of any securities to the Lien of this Indenture to the extent contemplated hereby.

SECTION 3.02. *Disposition of Payments on Pledged Property.*

Unless and until all Outstanding Securities have been paid in full or provision for the payment of such Securities has been made in accordance with this Indenture, the Trustee shall be entitled to receive all principal, premium (if any) and interest paid in respect of any Pledged Lessor Notes and interest paid on bonds or other obligations or indebtedness which may

be subject to the lien of this Indenture and shall apply the same to the payment of the principal of, and premium (if any) and interest on, the Securities when and as they become due and payable pursuant to, and in accordance with, this Indenture. The Trustee shall duly note on the Schedules attached to the Pledged Lessor Notes or by other appropriate means all payments of principal, premium, if any, and interest made on the Pledged Lessor Notes.

SECTION 3.03. *Exercise of Rights and Powers Under Pledged Lessor Notes and Lease Indentures.*

The Trustee shall not take any action as the holder of the Pledged Lessor Notes to direct any Lease Indenture Trustee in any respect or to vote any Pledged Lessor Note or any portion thereof except as specified in this Section. The Trustee shall give notice to the Securityholders of the occurrence of any event of default or default under any Lease Indenture, and of every Event of Loss or Deemed Loss Event occurring under a Lease, but only to the extent the same shall actually be known by an officer in the corporate trustee administration department of the Trustee. The Trustee may, at any time, and shall, upon the request of any Lease Indenture Trustee made to the Trustee to give any direction or to vote its interest in the Pledged Lessor Notes, request from Securityholders directions as to (i) whether or not to direct such Lease Indenture Trustee to take or refrain from taking any action which holders of a Pledged Lessor Note have the option to direct and (ii) how to vote any Pledged Lessor Note if a vote has been called for with respect thereto. In addition, any Securityholder may at any time request the Trustee to direct, or to participate in the direction of, any action under any Lease Indenture to the extent that the Trustee may do so under such Lease Indenture. Upon receiving from Securityholders any directions as to the taking or the refraining from taking, of any action, or the voting of any Pledged Lessor Note, the Trustee shall specify to the Lease Indenture Trustee the principal amount of the Pledged Lessor Note which is in favor of the action or vote, the principal amount of the Pledged Lessor Note which is opposed to the action or vote, and the principal amount of the Pledged Lessor Note which is not taking any position for the action or vote. Such principal amounts shall be determined by allocating the total principal amount of the Pledged Lessor Notes with respect to which direction is to be given the proportionate principal amount of Securities taking corresponding positions or not taking any position, based on the aggregate principal amount of Securities Outstanding. In addition, the

Trustee shall certify to the Lease Indenture Trustee that the principal amounts of Securities taking such corresponding positions or not taking any position was determined in accordance with the provisions of this Indenture.

SECTION 3.04. *Certain Actions in Case of Judicial Proceedings.*

In case all or any part of the property of any Lessor or any other Person which may be deemed an obligor in respect of the Pledged Lessor Notes shall be sold at any judicial or other involuntary sale, the Trustee shall receive any portion of the proceeds of such sale accruing on the Pledged Property held hereunder, and such proceeds shall be held as provided in Section 3.05.

SECTION 3.05. *Cash Held by Trustee Treated as a Deposit.*

Any and all cash held by the Trustee under any provision of this Indenture may be treated by the Trustee, until required to be paid out hereunder, as a deposit, in trust, without any liability for interest.

ARTICLE FOUR

WITHDRAWAL OF COLLATERAL.

SECTION 4.01. *Withdrawal of Collateral.*

Except as provided in Section 4.02 and Article Thirteen, none of the Pledged Property shall be subject to withdrawal unless and until all Outstanding Securities have been paid in full or provision for such payment has been made in accordance with the terms of this Indenture and the Trustee shall have received the documents and opinions required by Section 4.02 or Article Twelve.

SECTION 4.02. *Reassignment of Pledged Lessor Notes upon Payment.*

Upon receipt of payment in full of the principal of, and premium (if any) and interest on, any Pledged Lessor Note held by the Trustee, the Trustee shall deliver to the Company said Pledged Lessor Note and any instrument of transfer or assignment necessary to reassign to the Company said Pledged Lessor Note and the interest of the Company (if any) in the Lease Indenture relating thereto; provided that nothing herein contained shall prevent the Trustee from presenting any Pledged Lessor Note to a Lease Indenture Trustee for final payment in accordance with the applicable provisions of the related Lease Indenture.

ARTICLE FIVE

COVENANTS

SECTION 5.01. *Payment of Principal, Premium (if any) and Interest.*

The Company will duly and punctually pay, or cause to be paid, the principal of, and premium, if any, and interest on, the Securities in accordance with the terms of the Securities and this Indenture.

SECTION 5.02. *Maintenance of Office or Agency.*

The Company will maintain in the Borough of Manhattan, The City of New York, an office or agency where Securities may be presented or surrendered for payment, where Securities may be surrendered for transfer or exchange and where notices and demands to or upon the Company in respect of Securities and this Indenture may be served. The Paying Agent's Office is hereby designated as such office or agency. APS will give prompt written notice to the Trustee of the location, and of any change in the location, of each such office or agency. If at any time the Company shall fail to maintain any such office or agency or the Company or APS shall fail to furnish the Trustee with the address thereof, such presentations, surrenders, notices and demands may be made or served at the Corporate Trust Office of the Trustee, and the Company hereby appoints the Trustee its agent to receive all such presentations, surrenders, notices and demands.

SECTION 5.03. *Money for Security Payments to be Held in Trust.*

All moneys deposited with the Trustee or with any Paying Agent for the purpose of paying the principal of or premium, if any, or interest on Securities shall be deposited and held in trust for the benefit of the Holders of the Securities entitled to such principal, premium, if any, or interest, subject to the provisions of this Section. Moneys so deposited and held in trust shall not be a part of the Pledged Property but shall constitute a separate trust fund for the benefit of the Holders of the relevant Securities.

The Company may at any time, for the purpose of obtaining the satisfaction and discharge of this Indenture or for any other purpose, pay, or direct any Paying Agent to pay, to the Trustee all sums held in trust by such Paying Agent, such sums to be held by the Trustee upon the same trusts as those upon which such sums were held by such Paying Agent; 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 in trust for the payment of the principal of or premium, if any, or interest on any Security and remaining unclaimed for three years (or such lesser period as may be required by law to give effect to this provision) after such principal, premium or interest has become due and payable shall be paid to the Company on Company Request (to the extent such monies shall have been deposited by the Company) or to any other Person on its request (to the extent such monies shall have been deposited by such other Person); and the Holder of such Security shall thereafter, as an unsecured general creditor, look only to the Company or such other Person, to the extent such monies shall have been paid to the Company or such other Person, as the case may be, for payment thereof, and all liability of the Trustee or such Paying Agent with respect to such trust money shall thereupon cease; *provided, however*, that the Trustee or such Paying Agent, before being required to make any such repayment, may at the expense of the Company or, to the extent such monies are to be paid to another Person, such other Person cause to be mailed to each such Holder notice that such money remains unclaimed and that, after a date specified therein, which shall not be less than 30 days from the date of such mailing, any unclaimed balance of such money then remaining will be repaid to the Company or such other Person.

SECTION 5.04. *Maintenance of Corporate Existence.*

The Company, at its own cost and expense, will do or cause to be done all things necessary to preserve and keep in full force and effect its corporate existence, rights and franchises, except as otherwise specifically permitted in this Indenture; *provided, however*, that the Company shall not be required to preserve any right or franchise if the Board of Directors of the Company shall determine that the preservation thereof is no longer desirable in the conduct of the business of the Company and that the loss thereof is not disadvantageous in any material respect to the Securityholders.

SECTION 5.05. *Protection of Pledged Property.*

The Company and APS will from time to time execute and deliver all such supplements and amendments hereto and all such financing statements, continuation statements, instruments of further assurance, and other instruments necessary to

- (i) grant more effectively all or any portion of the Pledged Property,
- (ii) maintain or preserve the lien of this Indenture or carry out more effectively the purposes hereof,
- (iii) perfect, publish notice of, or protect the validity of, any grant made or to be made by this Indenture,
- (iv) enforce any of the Securities, or
- (v) preserve and defend title to any Securities or other instrument included in the Pledged Property and the rights of the Trustee, and of the Securityholders, in such Securities or other instrument against the claims of all persons and parties.

The Company and APS hereby designate the Trustee its agent and attorney-in-fact to execute any financing statement, continuation statement or other instrument required pursuant to this Section.

SECTION 5.06. *Opinions as to Pledged Property.*

Promptly after the execution and delivery of this Indenture and of each Series Supplemental Indenture or other supplemental indenture or other instrument of further assurance, the Company shall furnish to the Trustee an Opinion of Counsel stating that, in the opinion of such Counsel, this Indenture and all such Series Supplemental Indentures, other supplemental indentures and other instruments of further assurance have been properly recorded, registered and filed to the extent necessary to make effective the lien intended to be created by this Indenture, and reciting the details of such action or referring to prior Opinions of Counsel in which such details are given, and stating that all financing statements and continuation statements have been executed and filed that are necessary fully to preserve and protect the rights of the Securityholders and the Trustee, or stating that, in the opinion of such Counsel, no such action is necessary to make such lien effective.

On or before May 1, in each calendar year, beginning with the first calendar year commencing more than three months after the date of authentication and delivery of any Securities, the Company shall furnish to the Trustee an Opinion of Counsel either stating that, in the opinion of such counsel, such action has been taken with respect to the recording, filing, re-recording and re-filing of this Indenture, any Series Supplemental Inden-

ture and any other requisite documents and with respect to the execution and filing of any financing statements and continuation statements as is necessary to maintain the lien and security interest created by this Indenture with respect to the Pledged Property and reciting the details of such action or stating that in the opinion of such counsel no such action is necessary to maintain such lien and security interest. Such Opinion of Counsel shall also describe the recording, filing, re-recording and re-filing of this Indenture, any Series Supplemental Indenture and any other requisite documents and the execution and filing of any financing statements and continuation statements that will, in the opinion of such counsel, be required to maintain the lien and security interest of this Indenture with respect to the Pledged Property until May 1 in the following calendar year.

SECTION 5.07. *Performance of Obligations*

(a) Neither the Company nor APS will take any action or permit any action to be taken by others which would release any Person from any of such Person's covenants or obligations under any instrument included in the Pledged Property, or which would result in the amendment, hypothecation, subordination, termination or discharge of, or impair the validity or effectiveness of, any such instrument, except as expressly provided in this Indenture or such instrument.

(b) APS will fully perform all of its obligations under the Leases.

SECTION 5.08. *Negative Covenants.*

During such time as any Security issued hereunder is Outstanding, the Company will not:

(i) sell, transfer, exchange or otherwise dispose of any portion of the Pledged Property except as expressly permitted by this Indenture:

(ii) engage in any business or activity other than in connection with, or relating to, the issuance of Securities pursuant to this Indenture and application of the proceeds thereof as herein provided, or amend Article Third, Fourth or Sixth of its Certificate of Incorporation as in effect on the date of execution and delivery of this Indenture, without, in each case, the consent of the Holders of not less than 66⅔% of the aggregate principal amount of the Securities then Outstanding; notwithstanding the foregoing, however, the Company may, with respect to one or more series of Securities (or one or more Stated Maturities within any series), enter into credit or liquidity support

facilities (including, but without limitation, bank letters of credit, bank lines of credit and bonds of insurance);

(iii) issue bonds, notes or other evidences of indebtedness other than (A) Securities issued hereunder or (B) bonds, notes or other evidences of indebtedness permitted by clause (ii) above;

(iv) incur, assume or guaranty any indebtedness of any Person;

(v) dissolve or liquidate in whole or in part;

(vi) take any action which would (1) permit the validity or effectiveness of this Indenture or any grant of any of the Pledged Property to be impaired, or permit the Lien of this Indenture to be amended, hypothecated, subordinated, terminated or discharged, or permit any Person to be released from any covenant or obligation under this Indenture, (2) permit any lien, charge, security, mortgage or other encumbrance (other than the Lien of this Indenture) to be created on or extend to or otherwise arise upon or burden the Pledged Property or any part thereof or any interest therein or the proceeds thereof, or (3) permit the Lien of this Indenture not to constitute a valid first priority security interest in the Pledged Property; or

(vii) institute any proceedings to be adjudicated a bankrupt or insolvent, or consent to the institution of bankruptcy or insolvency proceedings against it, or file a petition or answer or consent seeking reorganization or relief under the Federal Bankruptcy Code or any other applicable federal or state law or law of the District of Columbia, or consent to the filing of any such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company or any substantial part of its property, or make an assignment for the benefit of its creditors, or admit in writing its inability to pay its debts generally as they become due, or take any corporate action in furtherance of the foregoing.

SECTION 5.09. *Administration of Principal Instruments.*

(a) Without the consent of the Holders of a majority in principal amount of Outstanding Securities, the Trustee shall not consent to any Change in any Principal Instrument; *provided, however*, that the Trustee may consent to any Change in any Principal Instrument if such Change is permitted by subsection (b) of this Section 5.09.

(b) Subject to the provisions of subsection (c) of this Section 5.09, the Trustee may consent to any Change in any Principal Instrument (it being understood that Changes in Principal Instruments other than the Pledged Lessor Notes do not require the Trustee's consent except to the extent that such requirement arises from the fact that the Trustee is a Holder of Pledged Lessor Notes) if such Change is:

(1) to cure any ambiguity, to correct or supplement any provision in such Principal Instrument which may be defective or inconsistent with any other provision in such Principal Instrument or any related Principal Instrument, or to make any other provisions with respect to matters arising under any such Principal Instrument, provided, in each instance, that such action shall not materially adversely affect the interests of Holders of Securities; or

(2) to add to the covenants and agreements of the parties to such Principal Instrument other covenants and agreements thereafter to be observed by any such party, or to surrender any right or power therein reserved to or conferred upon the Company; or

(3) to amend or supplement such Principal Instrument, or to give any consent or grant any waiver thereunder, so long as thereafter such Principal Instrument will comply with the requirements (if any) of Exhibit A hereto; *provided* that such action does not materially adversely affect the interests of Holders of Securities; or

(4) in any other manner not inconsistent with Exhibit A hereto; *provided* that such action does not materially adversely affect the interests of Holders of Securities; or

(5) a Change in the Lease permitted by applicable provisions of the related Lease Indenture; or

(6) to describe more fully and to amplify or correct the description of any property or rights assigned or pledged by such Principal Instrument or intended so to be, or to assign, pledge, mortgage or grant a security interest in any additional property, rights and interests, subject to such liens, restrictions or other encumbrances, if any, as shall be therein specifically described; or

(7) in the case of a Lease Indenture, to enable the Lease Indenture Trustee thereunder to confer upon holders of Pledged Lessor Notes any additional rights, remedies, powers or authorities that may lawfully be granted or conferred upon such holders; or

(8) to evidence the appointment of a separate or co-Lease Indenture Trustee or the succession of a new Lease Indenture Trustee; or

(9) to evidence the succession of or assumption by a successor or assignee Lessee under the Leases and the Participation Agreements or to evidence the succession of a new Lessor or Owner Trustee under any Principal Instrument to which it is a party; or

(10) permitted by the terms of such Principal Instrument to be made without the consent of or notice to the holders of the related Pledged Lessor Notes; or

(11) to provide for the issuance of Lessor Notes in addition to the Pledged Lessor Notes relating to such Principal Instruments in accordance with the applicable provisions of the related Principal Instruments.

(c) The Trustee shall not consent to any Change with respect to a Principal Instrument, whether effected pursuant to subsection (a) or pursuant to subsection (b) of this Section 5.09, anything in such subsections or elsewhere in this Indenture to the contrary notwithstanding, without the consent of the Holder of each Outstanding Security affected thereby if such Change would:

(1) except as provided in any Lease, change such Lease in such a way as to change the timing or reduce the amount of any Lease Payment, or otherwise to release, except as provided in such Lease, APS from its obligation under such Lease in respect of payment of Lease Payments; or

(2) modify, amend or supplement the Participation Agreements in such a way as to, or give any consent, waiver, authorization or approval which would, release any Equity Participant from its payment obligations contained in said Participation Agreements.

(d) Except during the continuance of an Event of Default hereunder, upon request of the Company or APS, the Trustee shall consent to any Change permitted by this Section 5.09 which requires the Trustee's consent, and shall execute any instrument requested by the Company or APS, as the case may be, for the purpose of confirming such consent, but only upon receipt by the Trustee of an Officers' Certificate and an Opinion of Counsel of the Company or APS, as the case may be, each stating that such Change is authorized by this Indenture and that execution of such instrument is appropriate to confirm such consent, unless such Change adversely affects the Trustee's rights, duties or immunities under this Indenture or other-

wise, in which case the Trustee may, in its discretion, but shall not be obligated to, give such consent, and the Trustee shall be fully protected in relying on such Officers' Certificate and Opinion of Counsel.

SECTION 5.10. *Annual Statement as to Compliance.*

(a) APS and the Company each will deliver to the Trustee, on or before 120 days after the end of each of its fiscal years, a written statement (which need not comply with Section 1.02) signed by its President or one of its Vice Presidents and by its Treasurer or one of its Assistant Treasurers or its Comptroller or one of its Assistant Comptrollers, stating, as to each signer thereof, that

(1) a review of the activities of APS or the Company, as the case may be, required during such year of APS or the Company, as the case may be, under this Indenture has been made under their supervision; and

(2) to the best of their knowledge, based on such review, APS or the Company, as the case may be, has fulfilled all its obligations under this Indenture throughout such year, or, if there has been a default in the fulfillment of any such obligation, specifying each such default known to such officer and the nature and status thereof.

(b) APS and the Company each will deliver to the Trustee, promptly after having obtained knowledge thereof, written notice of any event which with the giving of notice or lapse of time, or both, would become an Event of Default under Section 8.01.

SECTION 5.11. *Delivery of Certificate of Independent Public Accountant.*

APS will cause to be delivered to the Trustee any certificate of an independent public accountant (who shall not be an employee of the Company, APS or any Affiliate of either) delivered to any Lease Indenture Trustee pursuant to Section 2.4(c) of any Lease Indenture.

SECTION 5.12. *Delivery of Certificate of Engineer, Appraiser or Other Expert.*

In connection with any release from the security and other interest created by Section 2.1 of any Lease Indenture of a portion of the Lease Indenture Estate (as defined in such Lease Indenture) pursuant to Section 2.3 of such Lease Indenture, APS will cause to be delivered to the Trustee a certificate of an engineer, appraiser or other expert as the fair value of any portion of the Lease Indenture Estate to be released from the lien of such Lease Indenture and such certificate shall state that in the opinion of the

person making the same the proposed release will not impair the security under such Lease Indenture in contravention of the provisions thereof. If the fair value of the portion of the Lease Indenture Estate to be released and all other portions of the Lease Indenture Estate released since the commencement of the then current calendar year, as set forth in the certificate required pursuant to this Section 5.12, is ten per centum (10%) or more of the aggregate principal amount of Securities at the time Outstanding, such certificate shall be made by an independent engineer, appraiser or other expert; *provided, that*, a certificate of an independent engineer, appraiser, or other expert is not required in the case of any release of portions of the Lease Indenture Estate if the fair market value thereof as set forth in the certificate or opinion required by this Section 5.12 is less than \$25,000 or less than 1 per centum (1%) of the aggregate principal amount of Securities at the time Outstanding.

ARTICLE SIX

REDEMPTION OF SECURITIES

The provisions of this Article Six shall be applicable to the Securities of any series which are redeemable before their Stated Maturity of principal except as otherwise provided in such Securities or the Series Supplemental Indenture with respect thereto as contemplated by Section 2.03.

SECTION 6.01. *Notice to Trustee of Redemption.*

In case of any redemption of any Securities of any series otherwise than through the operation of an applicable Sinking Fund, the Company shall, at least 45 days prior to the scheduled Redemption Date (unless a shorter notice shall be satisfactory to the Trustee), notify the Trustee in writing of such Redemption Date and of the principal amount of Securities of such series to be redeemed.

SECTION 6.02. *Selection by Trustee of Securities to be Redeemed.*

If fewer than all the Securities of any series are to be redeemed, other than through the operation of an applicable Sinking Fund, the particular Securities of such series to be redeemed shall be selected following receipt by the Trustee of the notice required by Section 6.01, but not more than 60 days prior to the Redemption Date, by the Trustee, from the Outstanding Securities of such series not previously called for redemption, as follows. To the extent any Pledged Lessor Note is being prepaid in connection with such redemption, the Trustee shall first identify the Securities of such series having Stated Maturities of principal which correspond to the maturities (including serial maturities within a single Pledged Lessor

Note) of the Pledged Lessor Note being prepaid, and shall then identify the amounts which have been prepaid in respect of such maturity (or serial maturity) of Pledged Lessor Note. Following such identification, the Trustee shall select for redemption an aggregate principal amount of Securities of such series of each Stated Maturity of principal equal to the aggregate principal amount of the maturity (or serial maturity) of the Pledged Lessor Note being prepaid, such selection to be made by lot as among all Securities having such Stated Maturity of principal, according to such method as the Trustee shall deem proper in its discretion; *provided, however,* that when Securities are being redeemed pursuant to any applicable optional (rather than mandatory) redemption provisions, the Securities to be redeemed shall be selected solely from the Securities of the series and of the Stated Maturity of principal in respect of which a Company Order has been received. In any such designation by lot the designation may be made from the numbers of the Securities of such series then Outstanding (1) in groups of consecutive numbers (including or excluding, for the purpose of such grouping, the numbers of Securities previously called for redemption or otherwise retired), or (2) individually from the numbers of all such Securities not previously called for redemption or otherwise retired, or (3) if there is any portion to be called which is but a fraction of a group, individually by lot from the several individual numbers in any such group so designated by lot.

The Trustee shall promptly notify the Company, APS, the Security Registrar and each Paying Agent in writing of the Securities selected for redemption and, in the case of any Security selected for partial redemption, 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 Security redeemed or to be redeemed only in part, to the portion of the principal of such Security which has been or is to be redeemed.

SECTION 6.03. *Notice of Redemption.*

Notice of redemption (including redemption through the operation of any applicable Sinking Fund) shall be given by first-class mail, postage prepaid, mailed not less than 20 nor more than 60 days prior to the Redemption Date, to each Holder of Securities to be redeemed, at his address appearing in the Security Register.

All notices of redemption shall state:

- (1) the Redemption Date,
- (2) the Redemption Price,
- (3) if fewer than all Outstanding Securities of any series are to be redeemed, the identification (and, in the case of partial redemption, the respective principal amounts) of the particular Securities, including the series and the Stated Maturity of principal of such Securities, to be redeemed,
- (4) that on the Redemption Date the Redemption Price will become due and payable upon each such Security, and that interest thereon shall cease to accrue from and after said date,
- (5) the place where such Securities are to be surrendered for payment of the Redemption Price, and
- (6) that the redemption is through the operation of a Sinking Fund, if such is the case.

Notice of redemption of Securities to be redeemed shall be given by the Trustee in the name of the Company.

SECTION 6.04. *Deposit of Redemption Price.*

Prior to any Redemption Date, the Company shall deposit, or cause to be deposited, with the Paying Agent an amount of money sufficient to pay the Redemption Price of all the Securities which are to be redeemed on that date.

SECTION 6.05. *Securities Payable on Redemption Date.*

Notice of redemption having been given as aforesaid, the Securities so to be redeemed shall, on the Redemption Date, become due and payable at the corporate trust office of the Paying Agent (or, if such office is not in the Borough of Manhattan, the City of New York, at either such office or an office to be maintained in such Borough) at the Redemption Price therein specified and from and after such date (unless there shall be a default in the payment of the Redemption Price) such Securities shall cease to bear interest. Upon surrender of such Securities for redemption in accordance with said notice, such Securities shall be paid at the Redemption Price, *exclusive, however*, of installments of interest maturing on or prior to the Redemption Date, payment of which shall have been made or duly provided

for to the Holders of such Securities registered as such on the relevant Record Dates, or otherwise, according to their terms and the provisions of Section 2.10.

If any Security called for redemption shall not be so paid upon surrender thereof for redemption, the principal (and premium, if any) shall, until paid, continue to bear interest from the Redemption Date at the rate borne by the Security in respect of overdue payments.

SECTION 6.06. *Securities Redeemed in Part.*

Any Security which is to be redeemed only in part shall be surrendered at the corporate trust office of the Paying Agent (or, if such office is not in the Borough of Manhattan, the City of New York, at either such office or an office to be maintained in such Borough) (with due endorsement by, or a written instrument of transfer in form satisfactory to the Security Registrar duly executed by, the Holder thereof or his attorney duly authorized in writing) and the Company shall execute and the Trustee shall authenticate and deliver to the Paying Agent for delivery to the Holder of such Security a new Security or Securities of the same series and the same Stated Maturity of principal, of any authorized denomination as requested by such Holder in aggregate principal amount equal to and in exchange for the unredeemed portion of the principal of the Security so surrendered.

ARTICLE SEVEN

SINKING FUNDS

SECTION 7.01. *Sinking Funds for Securities.*

The amount of any sinking fund payment provided for by the terms of Securities of any series (and any Stated Maturity of principal within a series) is herein referred to as a "*Sinking Fund*", and the date on which a Sinking Fund payment is to be made is herein referred to as a "*Sinking Fund Date*." Each such Sinking Fund payment shall be applied to the redemption of Securities of the appropriate series and the appropriate Stated Maturity of principal on the appropriate Sinking Fund Date.

In the event that there shall have been any partial redemption of a series of Securities (other than pursuant to an applicable Sinking Fund), the Sinking Fund payments with respect to such series shall be adjusted as follows. The Trustee shall first identify the maturity (or serial maturity

within a Pledged Lessor Note) of the Pledged Lessor Note or Notes, if any, in respect of which a prepayment shall have been made and, having so identified such maturity, shall determine the dates on which the principal of such Pledged Lessor Notes were scheduled to be amortized (the "Scheduled Amortization Dates"). The aggregate amount of Sinking Fund payments scheduled to be made on a Sinking Fund Date shall then be adjusted to equal the aggregate principal amount of all Pledged Lessor Notes scheduled to be amortized on the Scheduled Amortization Date corresponding to such Sinking Fund Date, after taking into account the prepayment of Pledged Lessor Notes, and the amount of each Sinking Fund payment shall be proportionately adjusted. All such adjustments in respect of a Sinking Fund Date shall be rounded to the nearest \$1,000, and shall be subject to necessary further adjustment so that the total amount of such reduction is equal to the total principal amount of Securities redeemed pursuant to such partial redemption. In connection with such adjustments, the Company shall deliver to the Trustee a Company Request not later than 60 days prior to the next Sinking Fund Date following any partial redemption of a series of Securities (other than pursuant to an applicable Sinking Fund) setting forth a revised schedule of Sinking Fund payments applicable to such series of Securities. The Trustee may rely on such Company Request and shall have no duty with respect to the adjustments set forth therein other than to make them available for inspection by a Holder of such series of Securities at the Corporate Trust Office upon reasonable notice.

SECTION 7.02. *Selection by Trustee of Securities to Be Redeemed Through Operation of Sinking Fund.*

In the case of Securities to be redeemed through operation of an applicable Sinking Fund, the particular Securities to be redeemed shall be selected no more than 60 days nor less than 30 days prior to the Redemption Date by the Trustee from the Outstanding Securities of the same series and of the same Stated Maturity of principal not previously called for redemption by lot as among all Securities having such Stated Maturity. In any such designation by lot the designation may be made from the numbers of the Securities of such series then Outstanding (1) in groups of consecutive numbers (including or excluding, for the purpose of such grouping, the numbers of Securities previously called for redemption or otherwise retired), or (2) individually from the numbers of all such Securities not previously called for redemption or otherwise retired, or (3) if there is any

portion to be called which is but a fraction of a group, individually by lot from the several individual numbers in any such group so designated by lot.

ARTICLE EIGHT

EVENTS OF DEFAULT; REMEDIES

SECTION 8.01. *Events of Default.*

"Events of Default", wherever used herein, 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 a judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

(1) default in the payment of any interest upon any Security when it becomes due and payable, and continuance of such default for a period of ten (10) days; or

(2) default in the payment of the principal of (or premium, if any, on) any Security at its Stated Maturity, or upon call for redemption or otherwise, and continuance of such default for a period of ten (10) days; or

(3) default in the making of any Sinking Fund payment, and continuance of such default for a period of ten (10) days; or

(4) default in the performance, or breach, of any covenant of APS or the Company contained herein and continuance of such default or breach for a period of 30 days after there has been given, by registered or certified mail, to APS and the Company by the Trustee, or to APS, the Company and the Trustee by the Holders of at least 25% in principal amount of Outstanding Securities, a written notice specifying such failure and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder; or

(5) the occurrence of an "event of default" under any Lease Indenture; or

(6) the entry of a decree or order by a court having jurisdiction in the premises adjudging the Company a bankrupt or insolvent, or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition of or in respect of the Company under the Federal Bankruptcy Act or any other applicable federal or state

law or law of the District of Columbia, or appointing a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company or of any substantial part of its property, or ordering the winding up or liquidation of its affairs, and the continuance of any such decree or order unstayed and in effect for a period of 75 consecutive days; or

(7) the institution by the Company 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 the Federal Bankruptcy Code or any other applicable federal or state law or law of the District of Columbia, or the consent by it to the filing of any such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator (or other similar official) of the Company 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 corporate action by the Company in furtherance of any such action.

SECTION 8.02. *Acceleration of Maturity; Rescission and Annulment.*

Upon the occurrence of an Event of Default, (i) if such Event of Default is one referred to in clause (1), (2), (3), (4), (6) or (7) of Section 8.01, the Trustee may, and upon the direction of the Holders of not less than a majority in principal amount of the Securities Outstanding shall, and (ii) if such Event of Default is the one referred to in clause (5) of Section 8.01 (including without limitation an event of default under any Lease which has resulted in an Event of Default referred to in clause (1), (2), or (3) of Section 8.01) under circumstances in which the Pledged Lessor Notes have been declared immediately due and payable, the Trustee shall, declare the principal of all the Securities to be due and payable immediately, by a notice in writing to APS and the Company, and upon any such declaration such principal shall become immediately due and payable; provided that no such declaration shall be made (and no action under Section 8.03 or 8.05 shall be taken) in cases in which the Event of Default is one referred to in clause (1), (2), or (3) of Section 8.01 which resulted directly from a failure of APS to make any payment of rent under any Lease until such time as the Lessor under such Lease has been given the opportunity to exercise its rights, if any, under provisions of the related

Lease Indenture analogous to Section 6.8 of the Lease Indentures dated as of August 1, 1986.

At any time after such a declaration of acceleration has been made and before any sale of the Pledged Property, or any part thereof, shall have been made pursuant to any power of sale as hereinafter in this Article *provided*, the Holders of a majority in principal amount of the Securities Outstanding, by written notice to the Company and the Trustee, may rescind and annul such declaration and its consequences if

(1) there shall have been paid to or deposited with the Trustee a sum sufficient to pay

(A) all overdue installments of interest on all Securities,

(B) the principal of (and premium, if any, on) any Securities which have become due otherwise than by such declaration of acceleration and interest thereon at the respective rates provided in the Securities for late payments of principal or premium,

(C) to the extent that payment of such interest is lawful, interest upon overdue installments of interest at the respective rates provided in the Securities for late payments of interest, and

(D) all sums paid or advanced by the Trustee hereunder and the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel, and

(2) all Events of Default, other than the non-payment of the principal of Securities which have become due solely by such acceleration, have been cured or waived as provided in Section 8.08.

No such rescission shall affect any subsequent default or impair any right consequent thereon and no such annulment shall take place unless all declarations of acceleration of all Pledged Lessor Notes theretofore given have also been annulled in accordance with the terms of the applicable Lease Indentures.

Notwithstanding anything in this Section to the contrary, the Trustee shall rescind any declaration of maturity of the principal of and interest on the Securities as a consequence of an Event of Default which resulted from an event of default under any Lease and which resulted in a declaration of acceleration of the Pledged Lessor Notes issued under the related Lease Indenture, if the declaration of acceleration of such Lessor Notes has been

rescinded in accordance with the terms of such Lease Indenture and the conditions set forth in paragraphs (1) and (2) of this Section have been met.

SECTION 8.03. *Trustee's Power of Sale of Pledged Property; Notice Required; Power to Bring Suit.*

If an Event of Default shall have occurred and be continuing, subject to the provisions of Sections 8.06 and 8.07 and the proviso to the first paragraph of Section 8.02, the Trustee, by such officer or agent as it may appoint, may:

(1) sell, to the extent permitted by law, without recourse, for cash, or credit or for other property, for immediate or future delivery, and for such price or prices and on such terms as the Trustee in its discretion may determine, the Pledged Property as an entirety, or in any such portions as the Holders of a majority in aggregate principal amount of the Securities then Outstanding shall request by an Act of Securityholders, or, in the absence of such request, as the Trustee in its discretion shall deem expedient in the interest of the Securityholders, at public or private sale; and/or

(2) proceed by one or more suits, actions or proceedings at law or in equity or otherwise or by any other appropriate remedy, to enforce payment of the Securities or Pledged Lessor Notes, or to foreclose this Indenture or to sell the Pledged Property under a judgment or decree of a court or courts of competent jurisdiction, or by the enforcement of any such other appropriate legal or equitable remedy, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce any of its rights or powers or any of the rights or powers of the Securityholders.

In the event that the Trustee shall deem it advisable to sell any of or all the Pledged Property in accordance with the provisions of this Section, APS and the Company agree that if registration of any such Pledged Property shall be required, in the opinion of counsel for the Trustee, under the Securities Act of 1933 or other applicable law, and regulations promulgated thereunder, and if APS shall not effect, or cause to be effected, such registration promptly, the Trustee may sell any such Pledged Property at a private sale, and no Person shall attempt to maintain that the prices at which such Pledged Property is sold are inadequate by reason of the failure to sell at public sale, or hold the Trustee liable therefor.

SECTION 8.04. *Incidents of Sale of Pledged Property.*

Upon any sale of all or any part of the Pledged Property made either under the power of sale given under this Indenture or under judgment or decree in any judicial proceedings for foreclosure or otherwise for the enforcement of this Indenture, the following shall be applicable:

(1) *Securities Due and Payable.* The principal of, and premium, if any, and accrued interest on, the Securities, if not previously due, shall immediately become and be due and payable.

(2) *Trustee Appointed Attorney of Company to Make Conveyances.* The Trustee is hereby irrevocably appointed the true and lawful attorney of the Company, in its name and stead, to make all necessary deeds, bills of sale and instruments of assignment, transfer or conveyance of the property thus sold; and for that purpose the Trustee may execute all such documents and instruments and may substitute one or more persons with like power; and the Company hereby ratifies and confirms all that its said attorneys, or such substitute or substitutes, shall lawfully do by virtue hereof.

(3) *Company to Confirm Sales and Conveyances.* If so requested by the Trustee or by any purchaser, the Company shall ratify and confirm any such sale or transfer by executing and delivering to the Trustee or to such purchaser or purchasers all proper deeds, bills of sale; instruments of assignment, conveyance or transfer and releases as may be designated in any such request.

(4) *Securityholders and Trustee May Purchase Pledged Property.* Any Securityholder or the Trustee may bid for and purchase any of the Pledged Property, and upon compliance with the terms of sale, may hold, retain, possess and dispose of such Pledged Property in his or its own absolute right without further accountability.

(5) *Purchaser at Sale May Apply Securities to Purchase Price.* Any purchaser at any such sale may, in paying the purchase price, deliver any of the Securities then Outstanding in lieu of cash and apply to the purchase price the amount which shall, upon distribution of the net proceeds of such sale, after application to the costs of the action and any other sums which the Trustee is authorized to deduct under this Indenture, be payable on such Securities so delivered in respect of principal, premium, if any, and interest. In case the amount so payable on such Securities shall be less than the amount due

thereon, duly executed and authenticated Securities shall be delivered in exchange therefor to the Holder thereof for the balance of the amount due on such Securities so delivered by such Holder.

(6) *Receipt of Trustee Shall Discharge Purchaser.* The receipt of the Trustee or of the officer making such sale under judicial proceedings shall be a sufficient discharge to any purchaser for his purchase money, and, after paying such purchase money and receiving such receipt, such purchaser or his personal representative or assigns shall not be obliged to see to the application of such purchase money, or be in any way answerable for any loss, misapplication or non-application thereof.

(7) *Sale To Divest Rights of Company in Property Sold.* Any such sale shall operate to divest the Company of all right, title, interest, claim and demand whatsoever, either at law or in equity or otherwise, in and to the Pledged Property so sold, and shall be a perpetual bar both at law and in equity or otherwise against the Company, and its successors and assigns, and any and all persons claiming or who may claim the Pledged Property sold or any part thereof from, through or under the Company, or its successors and assigns.

(8) *Application of Moneys Received upon Sale.* Any moneys collected by the Trustee upon any sale made either under the power of sale given by this Indenture or under judgment or decree in any judicial proceedings for foreclosure or otherwise for the enforcement of this Indenture, shall be applied as provided in Section 8.12.

SECTION 8.05. *Judicial Proceedings Instituted by Trustee.*

(a) *Trustee May Bring Suit.* If there shall be a failure to make payment of the principal of any Security at its Stated Maturity or upon declaration of acceleration, call for redemption or otherwise, or of any Sinking Fund payment when due and payable by the terms hereof or of such Security, or if there shall be a failure to pay the premium, if any, or interest on any Security when the same becomes due and payable, then the Trustee, if any such failure shall continue for 15 days, in its own name, and as trustee of an express trust, shall be entitled, and empowered subject to the proviso to the first paragraph of Section 8.02 to institute any suits, actions or proceedings at law, in equity or otherwise, for the collection of the sums so due and unpaid on the Securities, and may prosecute any such claim or

proceeding to judgment or final decree, and may enforce any such judgment or final decree and collect the moneys adjudged or decreed to be payable in any manner provided by law, whether before or after or during the pendency of any proceedings for the enforcement of the Lien of this Indenture, or of any of the Trustee's rights or the rights of the Securityholders under this Indenture, and such power of the Trustee shall not be affected by any sale hereunder or by the exercise of any other right, power or remedy for the enforcement of the provisions of this Indenture or for the foreclosure of the lien hereof.

(b) *Trustee May Recover Unpaid Indebtedness after Sale of Pledged Property.* In the case of a sale of the Pledged Property and of the application of the proceeds of such sale to the payment of the indebtedness secured by this Indenture, the Trustee in its own name, and as trustee of an express trust, shall be entitled and empowered, by any appropriate means, legal, equitable or otherwise, to enforce payment of, and to receive all amounts then remaining due and unpaid upon, all or any of the Securities, for the benefit of the Holders thereof, and upon any other portion of the indebtedness remaining unpaid, with interest at the rates specified in the respective Securities on the overdue principal of and premium, if any, and (to the extent that payment of such interest is legally enforceable) on the overdue installments of interest.

(c) *Recovery of Judgment Does Not Affect Lien of this Indenture or Other Rights.* No recovery of any such judgment or final decree by the Trustee and no levy of any execution under any such judgment upon any of the Pledged Property, or upon any other property, shall in any manner or to any extent affect the Lien of this Indenture upon any of the Pledged Property, or any rights, powers or remedies of the Trustee, or any liens, rights, powers or remedies of the Securityholders, but all such liens, rights, powers and remedies shall continue unimpaired as before.

(d) *Trustee May File Proofs of Claim; Appointment of Trustee as Attorney-in-Fact in Judicial Proceedings.* The Trustee in its own name, or as trustee of an express trust, or as attorney-in-fact for the Securityholders, or in any one or more of such capacities (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 for the payment of overdue principal, premium (if any) or interest), shall be entitled and empowered to file such proofs of claim and other papers or documents as may be necessary or

advisable in order to have the claims of the Trustee and of the Securityholders (whether such claims be based upon the provisions of the Securities or of this Indenture) allowed in any equity, receivership, insolvency, bankruptcy, liquidation, readjustment, reorganization or any other judicial proceedings relative to the Company or any obligor on the Securities (within the meaning of the TIA), the creditors of the Company or any such obligor, the Pledged Property or any other property of the Company or any such obligor and any receiver, assignee, trustee, liquidator, sequestrator (or other similar official) in any such judicial proceeding is hereby authorized by each Securityholder 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 Securityholders, to pay to the Trustee any amount due to it for the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel. The Trustee is hereby irrevocably appointed (and the successive respective Holders of the Securities, by taking and holding the same, shall be conclusively deemed to have so appointed the Trustee) the true and lawful attorney-in-fact of the respective Securityholders, with authority to (i) make and file in the respective names of the Securityholders (subject to deduction from any such claims of the amounts of any claims filed by any of the Securityholders themselves), any claim, proof of claim or amendment thereof, debt, proof of debt or amendment thereof, petition or other document in any such proceedings and to receive payment of any amounts distributable on account thereof, (ii) execute any such other papers and documents and to do and perform any and all such acts and things for and on behalf of such Securityholders, as may be necessary or advisable in order to have the respective claims of the Trustee and of the Securityholders against the Company or any such obligor, the Pledged Property or any other property of the Company or any such obligor allowed in any such proceeding and (iii) receive payment of or on account of such claims and debt; *provided, however*, that nothing contained in this Indenture shall be deemed to give to the Trustee any right to accept or consent to any plan of reorganization or otherwise by action of any character in any such proceeding to waive or change in any way any right of any Securityholder. Any moneys collected by the Trustee under this Section shall be applied as provided in Section 8.12.

(e) *Trustee Need Not Have Possession of Securities.* All rights of action and of asserting claims under this Indenture or under any of the Securities enforceable by the Trustee may be enforced by the Trustee

without possession of any of such Securities or the production thereof at the trial or other proceedings relative thereto.

(f) *Suit To Be Brought for Ratable Benefit of Securityholders.* Any suit, action or other proceeding at law, in equity or otherwise which shall be instituted by the Trustee under any of the provisions of this Indenture shall be for the equal, ratable and common benefit of all the Securityholders, subject to the provisions of this Indenture.

(g) *Trustee May Be Restored to Former Position and Rights in Certain Circumstances.* In case the Trustee shall have proceeded to enforce any right under this Indenture by suit, foreclosure or otherwise and such proceedings shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee, then in every such case, APS, the Company and the Trustee shall be restored without further act to their respective former positions and rights hereunder, and all rights, remedies and powers of the Trustee shall continue as though no such proceedings had been taken.

SECTION 8.06. *Securityholders May Demand Enforcement of Rights by Trustee.*

If an Event of Default shall have occurred and shall be continuing, the Trustee shall, upon the written request of the Holders of a majority in aggregate principal amount of the Securities then Outstanding and upon the offering of indemnity as provided in Section 9.03(e), but subject in all cases to the provisions of Section 3.03 and the proviso to the first paragraph of Section 8.02, proceed to institute one or more suits, actions or proceedings at law, in equity or otherwise, or take any other appropriate remedy, to enforce payment of the principal of, or premium, if any, or interest on, the Securities or Pledged Lessor Notes or to foreclose this Indenture or to sell the Pledged Property under a judgment or decree of a court or courts of competent jurisdiction or under the power of sale herein granted, or take such other appropriate legal, equitable or other remedy, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce any of the rights or powers of the Trustee or the Securityholders, or, in case such Securityholders shall have requested a specific method of enforcement permitted hereunder, in the manner requested, provided that such action shall not be otherwise than in accordance with law and the provisions of this Indenture, and the Trustee, subject to such indemnity provisions, shall have the right to decline to follow any such request if the Trustee in good faith

shall determine that the suit, proceeding or exercise of the remedy so requested would involve the Trustee in personal liability or expense.

SECTION 8.07. *Control by Securityholders.*

The Holders of a majority in principal amount of the Outstanding Securities 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, provided that

(1) such direction shall not be in conflict with any rule of law or with this Indenture, and

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

SECTION 8.08. *Waiver of Past Defaults.*

The Holders of not less than a majority in principal amount of the Outstanding Securities may on behalf of the Holders of all the Securities waive any past default hereunder and its consequences, except that only the Holders of all Securities affected thereby may waive a default

(1) in the payment of the principal of (or premium, if any) or interest on such Securities, or

(2) in respect of a covenant or provision hereof which under Article Eleven cannot be modified or amended without the consent of the Holder of each Outstanding Security affected.

Upon any such waiver, such default shall cease to exist, and any Event 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 8.09. *Securityholder May Not Bring Suit Except under Certain Conditions.*

A Securityholder shall not have the right to institute any suit, action or proceeding at law or in equity or otherwise for the foreclosure of this Indenture, for the appointment of a receiver or for the enforcement of any other remedy under or upon this Indenture, unless:

(1) such Securityholder previously shall have given written notice to the Trustee of a continuing Event of Default;

(2) the Holders of at least 25% in aggregate principal amount of the Securities then Outstanding shall have requested the Trustee in writing to institute such action, suit or proceeding and shall have offered to the Trustee indemnity as provided in Section 9.03(e);

(3) the Trustee shall have refused or neglected to institute any such action, suit or proceeding for 60 days after receipt of such notice, request and offer of indemnity; and

(4) no direction inconsistent with such written request has been given to the Trustee during such 60-day period by the Holders of a majority in principal amount of Outstanding Securities.

It is understood and intended that no one or more of the Securityholders shall have any right in any manner whatever hereunder or under the Securities to (i) surrender, impair, waive, affect, disturb or prejudice the Lien of this Indenture on any property subject thereto or the rights of the Holders of any other Securities, (ii) obtain or seek to obtain priority or preference over any other such Holder or (iii) enforce any right under this Indenture, except in the manner herein provided and for the equal, ratable and common benefit of all the Securityholders subject to the provisions of this Indenture.

SECTION 8.10. *Undertaking To Pay Court Costs.*

All parties to this Indenture, and each Securityholder by his acceptance of a Security, shall be deemed to have agreed that any court may in its discretion require, in any suit, action or proceeding for the enforcement of any right or remedy under this Indenture, or in any suit, action or proceeding against the Trustee for any action taken or omitted by it as Trustee hereunder, the filing by any party litigant in such suit, action or proceeding of an undertaking to pay the costs of such suit, action or proceeding, and that such court may, in its discretion, assess reasonable costs, including reasonable attorneys' fees, against any party litigant in such suit, action or proceeding, having due regard to the merits *and good faith* of the claims or defenses made by such party litigant; provided, however, that the provisions of this Section shall not apply to (a) any suit, action or proceeding instituted by the Trustee, (b) any suit, action or proceeding instituted by any Securityholder or group of Securityholders

holding in the aggregate more than 10% in aggregate principal amount of the Securities then Outstanding or (c) any suit, action or proceeding instituted by any Securityholder for the enforcement of the payment of the principal of, or premium, if any, or interest on, any of the Securities, on or after the respective due dates expressed therein.

SECTION 8.11. *Right of Securityholders To Receive Payment Not To Be Impaired.*

Anything in this Indenture to the contrary notwithstanding, the right of any Holder of any Security to receive payment of the principal of, and premium, if any, and interest on, such Security, on or after the respective due dates expressed in such Security (or, in case of redemption, on the Redemption Date fixed for such Security), or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected without the consent of such Holder.

SECTION 8.12. *Application of Moneys Collected by Trustee.*

Any moneys collected or to be applied by the Trustee pursuant to this Article, together with any other moneys which may then be held by the Trustee under any of the provisions of this Indenture as security for the Securities (other than moneys at the time required to be held for the payment of specific Securities at their Stated Maturities or at a time fixed for the redemption thereof) shall be applied in the following order from time to time, on the date or dates fixed by the Trustee and, in the case of a distribution of such moneys on account of principal, premium, if any, or interest, upon presentation of the several Outstanding Securities, and stamping thereon of payment, if only partially paid, and upon surrender thereof, if fully paid:

FIRST: to the payment of all taxes, assessments or liens prior to the Lien of this Indenture, except those subject to which any sale shall have been made, all reasonable costs and expenses of collection, including the reasonable costs and expenses of handling the Pledged Property and of any sale thereof pursuant to the provisions of this Article and of the enforcement of any remedies hereunder or under any Lease Indenture, and to the payment of all amounts due the Trustee or any predecessor Trustee under Section 9.07, or through the Trustee by any Securityholder or Securityholders;

SECOND: in case the principal of the Securities or any of them shall not have become due, to the payment of any interest in default, in the order of the maturity of the installments of such interest, with interest at the rates specified in the respective Securities in respect of overdue payments (to the extent that payment of such interest shall be legally enforceable) on the overdue installments thereof;

THIRD: in case the principal of any of but not all the Securities shall have become due at their Stated Maturities, upon redemption or otherwise, first to the payment of accrued interest in the order of the maturity of the installments thereof with interest at the respective rates specified in the Securities in respect of payments on overdue principal, premium, if any, and (to the extent that payment of such interest shall be legally enforceable) on overdue installments of interest, and next to the payment of the principal of all Securities then due;

FOURTH: in case the principal of all the Securities shall have become due at their Stated Maturities, by declaration, upon redemption or otherwise, to the payment of the whole amount then due and unpaid upon the Securities then Outstanding for principal, premium, if any, and interest, together with interest at the respective rates specified in the Securities in respect of overdue payments on principal, premium, if any, and (to the extent that payment of such interest shall be legally enforceable) on overdue installments of interest, and, in case such proceeds shall be insufficient to pay in full the whole amount so due and unpaid, then to the payment of such principal, premium, if any, and interest ratably, without discrimination or preference; and

FIFTH: in case the principal of all the Securities shall have become due at their Stated Maturities, by declaration, upon redemption or otherwise, and all of such Securities shall have been fully paid, together with all interest (including any interest on overdue payments) and premium, if any, thereon, any surplus then remaining shall be paid to the Company, its successors or assigns, or to whomsoever may be lawfully entitled to receive the same, or as a court of competent jurisdiction may direct;

provided, however, that all payments to be made pursuant to this Section shall be made ratably to the persons entitled thereto, without discrimination or preference.

SECTION 8.13. *Securities Held by Certain Persons Not To Share in Distribution.*

Any Securities known to the Trustee to be owned or held by, or for the account or benefit of, APS, the Company or any Affiliate of any thereof shall not be entitled to share in any payment or distribution provided for in this Article until all Securities held by other Persons have been paid in full.

SECTION 8.14. *Waiver of Appraisement, Valuation, Stay, Right to Marshalling.*

To the extent it may lawfully do so, each of APS and the Company, for itself and for any Person who may claim through or under it, hereby:

(1) agrees that neither it nor any such Person will set up, plead, claim or in any manner whatsoever take advantage of, any appraisement, valuation, stay, extension or redemption laws, now or hereafter in force in any jurisdiction, which may delay, prevent or otherwise hinder (i) the performance or enforcement or foreclosure of this Indenture, (ii) the sale of any of the Pledged Property, or (iii) the putting of the purchaser or purchasers thereof into possession of such property immediately after the sale thereof;

(2) waives all benefit or advantage of any such laws;

(3) waives and releases all rights to have the Pledged Property marshalled upon any foreclosure, sale or other enforcement of this Indenture; and

(4) consents and agrees that all the Pledged Property may at any such sale be sold by the Trustee as an entirety.

SECTION 8.15. *Remedies Cumulative; Delay or Omission Not a Waiver.*

Every remedy given hereunder to the Trustee or to any of the Securityholders shall not be exclusive of any other remedy or remedies, and every such remedy shall be cumulative and in addition to every other remedy given hereunder or now or hereafter given by statute, law, equity or otherwise. The Trustee may exercise all or any of the powers, rights or remedies given to it hereunder or which may now or hereafter be given by statute, law or equity or otherwise, in its absolute discretion. No course of dealing between APS or the Company and the Trustee or the Securityholders or any delay or omission of the Trustee or of any Securityholder to exercise any right, remedy or power accruing upon any Event of Default

shall impair any such right, remedy or power or shall be construed to be a waiver of any such Event of Default or of any right of the Trustee or of the Securityholders or acquiescence therein, and, subject to the provisions of Section 8.07, every right, remedy and power given by this Article to the Trustee or to the Securityholders may be exercised from time to time and as often as may be deemed expedient by the Trustee or by the Securityholders.

ARTICLE NINE

THE TRUSTEE

SECTION 9.01. *Certain Duties and Responsibilities.*

(a) Except during the continuance of an Event of Default,

(1) the Trustee undertakes to perform 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

(2) in the absence of bad faith on its part, the Trustee may 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 has occurred and is continuing, the Trustee shall exercise 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

(1) this Subsection shall not be construed to limit the effect of Subsection (a) of this Section;

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

(3) 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 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; and

(4) 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 herein 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 9.02. *Notice of Defaults.*

In addition to its obligation to give notice to Securityholders as provided in Section 3.03, as promptly as practicable after, and in any event within 90 days after, the occurrence of any default hereunder, the Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, notice of such default hereunder actually known by an officer in the corporate trustee administration department of the Trustee, unless such default shall have been cured or waived; *provided, however,* that, except in the case of a default in the payment of the principal of (or premium, if any) or interest on any Security or in the payment of any Sinking Fund installment, the 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 Trustee in good faith determine that the withholding of such notice is in the interests of the Securityholders; and *provided, further,* that in the case of any default of the character specified in Section 8.01(4) no such notice to Securityholders shall be given until at least 30 days after the occurrence

thereof. 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 9.03. *Certain Rights of Trustee.*

Except as otherwise provided in Section 9.01:

(a) the Trustee may rely and shall be protected in acting or refraining from acting in reliance upon any resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order, bond, debenture 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) any request or direction of APS or the Company mentioned herein shall be sufficiently evidenced by an APS or Company Request or Order, in the case of a request or direction of APS, the Company, as the case may be and any resolution of the Board of Directors of APS or the Company may be sufficiently evidenced by a Board Resolution of APS or the Company, as the case may be;

(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 be herein specifically prescribed) may, in the absence of bad faith on its part, rely upon an Officers' Certificate of APS or the Company;

(d) the Trustee may consult with counsel and the 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 of the Securityholders pursuant to this Indenture, unless such Securityholders shall have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities which might be incurred by it in compliance 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 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 be entitled to examine the books, records and premises of APS or the Company, personally or by agent or attorney; and

(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.

SECTION 9.04. *Not Responsible for Recitals or Issuance of Securities.*

The recitals contained herein and in the Securities, except the certificates of authentication, shall not be taken as the statements of the Trustee, and the Trustee assumes no responsibility for their correctness. The Trustee makes no representations as to the validity or sufficiency of this Indenture, the Pledged Property or the Securities, except that the Trustee hereby represents and warrants that this Indenture has been executed and delivered by one of its officers who is duly authorized to execute and deliver such document on its behalf. The Trustee shall not be accountable for the use or application by the Company of Securities or the proceeds thereof.

SECTION 9.05. *May Hold Securities.*

The Trustee, any Paying Agent, Security Registrar or any other agent of APS or the Company, in its individual or any other capacity, may become the owner or pledgee of Securities and, subject to Sections 9.08 and 9.13, may otherwise deal with APS and the Company with the same rights it would have if it were not Trustee, Paying Agent, Security Registrar or such other agent.

SECTION 9.06. *Funds May Be Held by Trustee or Paying Agent; Investments.*

(a) Subject to subsection (b) of this Section 9.06, any monies held by the Trustee or the Paying Agent hereunder as part of the Pledged Property

may, until paid out by the Trustee or the Paying Agent as herein provided, be carried by the Trustee or the Paying Agent on deposit with itself, and neither the Trustee nor the Paying Agent shall have any liability for interest upon any such monies.

(b) At any time and from time to time prior to payment in full of any amounts to be paid by the Trustee pursuant to Section 2.15(b) in respect of any series of Securities (or prior to payment in full of any amount required to be paid by the Trustee in respect of such series of Securities pursuant to the applicable provisions of the Series Supplemental Indenture relating thereto if such series of Securities is to be authenticated in advance of the actual delivery to the Trustee of the Pledged Lessor Notes relating thereto) if at the time no Event of Default has occurred and is continuing, the Trustee shall, on Company Request, invest and reinvest in Permitted Investments as specified in such Company Request any monies from the sale of the Securities of such series at the time on deposit with the Trustee as part of the Pledged Property, together with any income and gains from the investment and reinvestment thereof, and sell any Permitted Investments, in either case, at such prices, including accrued interest, as are set forth in such Company Request, and such Permitted Investments shall be held by the Trustee until so sold in trust as part of the Pledged Property. The Trustee shall, on Company Request, sell such Permitted Investments as may be specified therein, and the Trustee shall, without Company Request, in the event monies are required for payment of any amounts to be paid by the Trustee pursuant to Section 2.15(b) in respect of any series of Securities and for any Stated Maturity of any installment of interest on any series of Securities becoming due and payable prior to the thirtieth day following the Termination Date applicable to such series, sell such Permitted Investments as are required to restore to cash as part of the Pledged Property such amounts as are needed for any such payment. The Trustee shall not be responsible for any losses on any investments or sales of Permitted Investments made pursuant to the procedure specified in this subsection (b).

Section 9.07. *Compensation and Reimbursement.*

The Company agrees

(1) to pay, or cause to be paid, to each of the Trustee and any Authorized Agent 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);

(2) to reimburse, or cause to be reimbursed, each of the Trustee and any Authorized Agent upon its request for all expenses, disbursements and advances incurred or made by it in accordance with any provision of this Indenture (including the compensation and the expenses and disbursements of its agents and counsel), except any such expense, disbursement or advance as may be attributable to its own negligence, willful misconduct or bad faith; and

(3) to indemnify, or cause to be indemnified, each of the Trustee, any predecessor Trustee and any Authorized Agent for, and to hold it harmless against, any loss, liability or expense incurred without negligence, willful misconduct or bad faith on its part, arising out of or in connection with the acceptance or administration of this trust or the performance of its duties hereunder, including the 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.

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, except funds held in trust for the payment of principal of (and premium, if any) or interest on particular Securities.

SECTION 9.08. *Disqualification; Conflicting Interests.*

(a) If the Trustee has or shall acquire any conflicting interest, as defined in this Section, it shall, within 90 days after ascertaining that it has such conflicting interest, either eliminate such conflicting interest or resign in the manner and with the effect hereinafter specified in this Article.

(b) In the event that the Trustee shall fail to comply with the provisions of Subsection (a) of this Section the Trustee shall, within 10 days after the expiration of such 90-day period, transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, notice of such failure.

(c) For the purposes of this Section, the Trustee shall be deemed to have a conflicting interest if

(1) the Trustee is trustee under another Indenture under which any other securities, or certificates of interest or participation in any

other securities, of any obligor on the Securities are outstanding, unless (A) the Securities are collateral trust bonds under which the only collateral consists of securities issued under such other indenture, or (B) such other indenture is a collateral trust indenture under which the only collateral consists of Securities issued under this Indenture, provided that there shall be excluded from the operation of this paragraph any indenture or indentures under which other securities, or certificates of interest or participation in other securities, of such obligor are outstanding, if such obligor shall have sustained the burden of proving, on application to the Commission and after opportunity for hearing thereon, that trusteeship under this Indenture and such other indenture or indentures is not so likely to involve a material conflict of interest as to make it necessary in the public interest or for the protection of investors to disqualify the Trustee from acting as such under one of such indentures;

(2) the Trustee or any of its directors or executive officers is an obligor upon the Securities or an underwriter for such obligor;

(3) the Trustee directly or indirectly controls or is directly or indirectly controlled by or is under direct or indirect common control with any obligor on the Securities or an underwriter for such obligor;

(4) the Trustee or any of its directors or executive officers is a director, officer, partner, employee, appointee or representative of any obligor on the Securities, or of an underwriter (other than the Trustee itself) for such obligor who is currently engaged in the business of underwriting, except that (i) one individual may be a director or an executive officer, or both, of the Trustee and a director or an executive officer, or both, of an obligor on the Securities but may not be at the same time an executive officer of both the Trustee and such obligor; (ii) if and so long as the number of directors of the Trustee in office is more than nine, one additional individual may be director or an executive officer, or both, of the Trustee and a director of an obligor on the Securities; and (iii) the Trustee may be designated by an obligor on the Securities or by any underwriter for such obligor to, act in the capacity of transfer agent, registrar, custodian, paying agent, fiscal agent, escrow agent, or depository, or in any other similar capacity, or, subject to the provisions of paragraph (1) of this Subsection, to act as trustee, whether under an indenture or otherwise;

(5) 10% or more of the voting securities of the Trustee is beneficially owned either by any director, partner, or executive officer thereof, or 20% or more of such voting securities is beneficially owned, collectively, by any two or more of such persons; or 10% or more of the voting securities of the Trustee is beneficially owned either by an underwriter for any obligor on the Securities or by any director, partner or executive officer thereof, or is beneficially owned collectively by any two or more such persons;

(6) the Trustee is the beneficial owner of, or holds as collateral security for an obligation which is in default (as hereinafter in this Subsection defined), (i) 5% or more of the voting securities, or 10% or more of any other class of security, of any obligor on the Securities not including the Securities issued under this Indenture and securities issued under any other indenture under which the Trustee is also trustee, or (ii) 10% or more of any class of security of an underwriter for any obligor on the Securities;

(7) the Trustee is the beneficial owner of, or holds as collateral security for an obligation which is in default (as hereinafter in this Subsection defined), 5% or more of the voting securities of any person who, to the knowledge of the Trustee, owns 10% or more of the voting securities of, or controls directly or indirectly or is under direct or indirect common control with, any obligor on the Securities;

(8) the Trustee is the beneficial owner of, or holds collateral security for an obligation which is in default (as hereinafter in this Subsection defined), 10% or more of any class of security of any person who, to the knowledge of the Trustee, owns 50% or more of the voting securities of any obligor on the Securities; or

(9) the Trustee owns, on May 15 in any calendar year, in the capacity of executor, administrator, testamentary or inter vivos trustee, guardian, committee or conservator, or in any other similar capacity, an aggregate of 25% or more of the voting securities, or of any class of security, of any person, the beneficial ownership of a specified percentage of which would have constituted a conflicting interest under paragraphs (6), (7) or (8) of this Subsection. As to any such securities of which the Trustee acquired ownership through becoming executor, administrator, or testamentary trustee of an estate which included them, the provisions of the preceding sentence shall not apply, for a period of two years from the date of such acquisition to the

extent that such securities included in such estate do not exceed 25% of such voting securities or 25% of any such class of security. Promptly after May 15 in each calendar year, the Trustee shall make a check of its holdings of such securities in any of the above mentioned capacities as of such May 15. If any obligor upon the Securities' fails to make payment in full of the principal of, or the premium, if any, or interest on, any of the Securities when and as the same becomes due and payable, and such failure continues for 30 days thereafter, the Trustee shall make a prompt check of its holdings of such securities in any of the above mentioned capacities as of the date of the expiration of such 30 day period, and after such date, notwithstanding the foregoing provisions of this paragraph, all such securities so held by the Trustee, with sole or joint control over such securities vested in it, shall, but only so long as such failure shall continue, be considered as though beneficially owned by the Trustee for the purposes of paragraphs (6), (7) and (8) of this Subsection.

The specification of percentages in paragraphs (5) to (9) inclusive, of this Subsection, shall not be construed as indicating that the ownership of such percentages of the securities of a person is or is not necessary or sufficient to constitute direct or indirect control for the purposes of paragraph (3) or (7) of this Subsection.

For the purposes of paragraphs (6), (7), (8) and (9) of this Subsection only, (i) the terms "security" and "securities" shall include only such securities as are generally known as corporate securities, but shall not include any note or other evidence of indebtedness issued to evidence an obligation to repay moneys loaned to a person by one or more banks, trust companies or banking firms, or any certificate of interest or participation in any such note or evidence of indebtedness; (ii) an obligation shall be deemed to be "in default" when a default in payment of principal shall have continued for 30 days or more and shall not have been cured; and (iii) the Trustee shall not be deemed to be the owner or holder of (A) any security which it holds as collateral security, as trustee or otherwise, for an obligation which is not in default as defined in clause (ii) above, or (B) any security which it holds as collateral security under this Indenture, irrespective of any default hereunder, or (C) any security which it holds as agent for collection, or as custodian, escrow agent, or depositary, or in any similar representative capacity.

Except as provided in the next preceding paragraph, the word "security" or "securities" as used in this Indenture shall mean any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit sharing agreement, collateral trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to purchase, any of the foregoing.

(d) For the purposes of this Section:

(1) The term "underwriter" when used with reference to any obligor on the Securities means every person who, within three years prior to the time as of which the determination is made, has purchased from such obligor with a view to, or has offered or sold for such obligor in connection with, the distribution of any security of such obligor outstanding at such time, or has participated or has had a direct or indirect participation in any such undertaking, or has participated or has had a participation in the direct or indirect underwriting of any such undertaking, but such term shall not include a person whose interest was limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission.

(2) The term "director" means any director of a corporation, or any individual performing similar functions with respect to any organization whether incorporated or unincorporated.

(3) The term "person" means an individual, a corporation, a partnership, an association, a joint-stock company, a trust, an unincorporated organization, or a government or political subdivision thereof. As used in this paragraph, the term "trust" shall include only a trust where the interest or interests of the beneficiary or beneficiaries are evidenced by a security.

(4) The term "voting security" means any security presently entitling the owner or holder thereof to vote in the direction or management of the affairs of a person, or any security issued under or pursuant to any trust, agreement or arrangement whereby a trustee or

trustees or agent or agents for the owner or holder of such security are presently entitled to vote in the direction or management of the affairs of a person.

(5) The term "obligor" means any obligor upon the Securities within the meaning of TIA.

(6) The term "executive officer" means the president, every vice president, every trust officer, the cashier, the secretary, and the treasurer of a corporation, and any individual customarily performing similar functions with respect to any organization whether incorporated or unincorporated, but shall not include the chairman of the board of directors.

(e) The percentages of the voting securities and other securities specified in this Section shall be calculated in accordance with the following provisions:

(1) A specified percentage of the voting securities of the Trustee, any obligor or any other person referred to in this Section (each of whom is referred to as a "person" in this paragraph) means such amount of the outstanding voting securities of such person as entitles the holder or holders thereof to cast such specified percentage of the aggregate votes which the holders of all the outstanding voting securities of such person are entitled to cast in the direction or management of the affairs of such person.

(2) A specified percentage of a class of securities of a person means such percentage of the aggregate amount of securities of the class outstanding.

(3) The term "amount", when used in regard to securities, means the principal amount if relating to evidences of indebtedness, the number of shares if relating to capital shares and the number of units if relating to any other kind of security.

(4) The term "outstanding" means issued and not held by or for the account of the issuer. The following securities shall not be deemed outstanding within the meaning of this definition:

(i) securities of an issuer held in a sinking fund relating to securities of the issuer of the same class;

(ii) securities of an issuer held in a sinking fund relating to another class of securities of the issuer, if the obligation evidenced by such other class of securities is not in default as to principal or interest or otherwise;

(iii) securities pledged by the issuer thereof as security for an obligation of the issuer not in default as to principal or interest or otherwise; and

(iv) securities held in escrow if placed in escrow by the issuer thereof;

provided, however, that any voting securities of an issuer shall be deemed outstanding if any person other than the issuer is entitled to exercise the voting rights thereof.

(5) A security shall be deemed to be of the same class as another security if both securities confer upon the holder or holders substantially the same rights and privileges; *provided, however,* that in the case of secured evidences of indebtedness, all of which are issued under a single indenture, differences in the interest rates or maturity dates of various series thereof shall not be deemed sufficient to constitute such series different classes; and *provided, further,* that, in the case of unsecured evidences of indebtedness, differences in the interest rates or maturity dates thereof shall not be deemed sufficient to constitute them securities of different classes, whether or not they are issued under a single indenture.

SECTION 9.09. *Corporate Trustee Required; Eligibility.*

There shall at all times be a Trustee hereunder which shall be a corporation organized and doing business under the laws of the United States of America or of any State, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least \$50,000,000, and subject to supervision or examination by Federal or State authority. If such corporation publishes reports of condition at least annually, pursuant to law or to the requirements of the aforesaid 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, it shall resign immediately in the manner and with the effect hereinafter specified in this Article.

SECTION 9.10. *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 under Section 9.11.

(b) The Trustee may resign at any time by giving written notice thereof to APS and the Company. If an instrument of acceptance by a successor Trustee shall not have been delivered to APS, the Company and the Trustee within 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.

(c) The Trustee may be removed at any time by Act of the Holders of a majority in principal amount of the Outstanding Securities, delivered to the Trustee, APS and to the Company.

(d) If at any time:

(i) the Trustee shall fail to comply with Section 9.08(a) after written request therefor by any Lessor or by any Securityholder who has been a bona fide Holder of a Security for at least 6 months, or

(ii) the Trustee shall cease to be eligible under Section 9.09 and shall fail to resign after written request therefor by any Lessor or by any such Securityholder, 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, (i) APS, acting after consultation with the Company, may remove the Trustee by Board Resolution or (ii) subject to Section 8.10, any Securityholder who has been a bona fide Holder of a Security for at least 6 months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the removal of the Trustee and the appointment of a successor Trustee.

(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, APS, acting after consultation with the Company, shall promptly appoint by Board Resolution a successor Trustee. If, within 1 year after such resignation, removal or incapability, or the occurrence of such vacancy, a successor Trustee shall be appointed by Act of the Holders of a majority in principal amount of the Outstanding Securities delivered to APS, the Company and the retiring Trustee, the successor Trustee so appointed shall, forthwith upon its acceptance of such appointment, become the successor Trustee and supersede the successor Trustee appointed by APS. If no successor Trustee shall have been so appointed by APS, acting after consultation with the Company, or by the Securityholders, and accepted appointment in the manner hereinafter provided, any Securityholder who has been a bona fide Holder of a Security for at least 6 months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the appointment of a successor Trustee.

(f) The Company shall give notice of each resignation and each removal of the Trustee and each appointment of a successor Trustee by mailing written notice of such event by first-class mail, postage prepaid, to the Holders of Securities as their names and addresses appear in the Security Register. Each notice shall include the name of the successor Trustee and the address of its Corporate Trust Office.

SECTION 9.11. *Acceptance of Appointment by Successor.*

Every successor Trustee appointed hereunder shall execute, acknowledge and deliver to APS, 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, deed or conveyance, shall become vested with all the rights, powers, trusts and duties of the retiring Trustee; but, on request of any Lessor, the Company or the successor Trustee, such retiring Trustee shall, upon payment of its charges, 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, subject nevertheless to its lien, if any, provided for in Section 9.07. Upon request of any such successor Trustee, APS and the Company shall execute any and all instruments for more fully and certainly

vesting in and confirming to such successor Trustee all such rights, powers and trusts.

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 9.12. *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 of 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 9.13. *Preferential Collection of Claims against any Obligor.*

(a) Subject to Subsection (b) of this Section, if the Trustee shall be or shall become a creditor, directly or indirectly, secured or unsecured, of any obligor on the Securities (as defined in Subsection (c) of this Section) within 4 months prior to a default, as defined in Subsection (c) of this Section, or subsequent to such a default, then, unless and until such default shall be cured, the Trustee shall set apart and hold in a special account for the benefit of the Trustee individually, the Holders of the Securities and the holders of other indenture securities (as defined in Subsection (c) of this Section):

(i) an amount equal to any and all reductions in the amount due and owing upon any claim as such creditor in respect of principal or interest, effected after the beginning of such 4 month period and valid as against any obligor on the Securities and its other creditors, except any such reduction resulting from the receipt or disposition of any property described in paragraph (ii) of this Subsection, or from the exercise of any right of set-off which the Trustee could have exercised if

a petition in bankruptcy had been filed by or against any such obligor upon the date of such default; and (ii) all property received by the Trustee in respect of any claim as such creditor, either as security therefor, or in satisfaction or composition thereof, or otherwise, after the beginning of such 4 month period, or an amount equal to the proceeds of any such property, if disposed of, subject, however, to the rights, if any, of any obligor on the Securities and its other creditors in such property or such proceeds.

Nothing herein contained, however, shall affect the right of the Trustee

(A) to retain for its own account (i) payments made on account of any such claim by any Person (other than an obligor on the Securities) who is liable thereon, and (ii) the proceeds of the bona fide sale of any such claim by the Trustee to a third person, and (iii) distributions made in cash, securities or other property in respect of claims filed against such obligor in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law;

(B) to realize, for its own account, upon any property held by it as security for any such claim, if such property was so held prior to the beginning of such 4 month period;

(C) to realize, for its own account, but only to the extent of the claim hereinafter mentioned, upon any property held by it as security for any such claim, if such claim was created after the beginning of such 4 month period and such property was received as security therefor simultaneously with the creation thereof, and if the Trustee shall sustain the burden of proving that at the time such property was so received the Trustee had no reasonable cause to believe that a default as defined in Subsection (c) of this Section would occur within 4 months; or

(D) to receive payment on any claim referred to in paragraph (B) or (C), against the release of any property held as security for such claim as provided in paragraph (B) or (C), as the case may be, to the extent of the fair value of such property.

For the purposes of paragraphs (B), (C) and (D), property substituted after the beginning of such 4 month period for property held as security at the time of such substitution shall, to the extent of the fair value of the property released, have the same status as the property released, and, to the

extent that any claim referred to in any of such paragraphs is created in renewal of or in substitution for or for the purpose of repaying or refunding any pre-existing claim of the Trustee as such creditor, such claim shall have the same status as such pre-existing claim.

If the Trustee shall be required to account, the funds and property held in such special account and the proceeds thereof shall be apportioned between the Trustee, the Securityholders and the holders of other indenture securities in such manner that the Trustee, the Securityholders and the holders of other indenture securities realize, as a result of payments from such special account and payments of dividends on claims filed against the obligor on the Securities in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, the same percentage of their respective claims, figured before crediting to the claim of the Trustee anything on account of the receipt by it from such obligor of the funds and property in such special account and before crediting to the respective claims of the Trustee and the Securityholders and the holders of other indenture securities dividends on claims filed against such obligor in bankruptcy or receivership or in proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, but after crediting thereon receipts on account of the indebtedness represented by their respective claims from all sources other than from such dividends and from the funds and property so held in such special account. As used in this paragraph, with respect to any claim, the term "dividends" shall include any distribution with respect to such claim, in bankruptcy or receivership or proceedings for reorganization pursuant to the Federal Bankruptcy Act or applicable State law, whether such distribution is made in cash, securities, or other property, but shall not include any such distribution with respect to the secured portion, if any, of such claim. The court in which such bankruptcy, receivership or proceedings for reorganization is pending shall have jurisdiction (i) to apportion between the Trustee and the Securityholders and the holders of other indenture securities, in accordance with the provisions of this paragraph, the funds and property held in such special account and proceeds thereof, or (ii) in lieu of such apportionment, in whole or in part, to give to the provisions of this paragraph due consideration in determining the fairness of the distributions to be made to the Trustee and the Securityholders and the holders of other indenture securities with respect to their respective claims, in which event it shall not be necessary to liquidate or to appraise the value of any securities or other property held in such special account or as security

for any such claim, or to make a specific allocation of such distributions as between the secured and unsecured portions of such claims, or otherwise to apply the provisions of this paragraph as a mathematical formula.

Any Trustee which has resigned or been removed after the beginning of such 4 month period shall be subject to the provisions of this Subsection as though such resignation or removal had not occurred. If any Trustee has resigned or been removed prior to the beginning of such 4 month period, it shall be subject to the provisions of this Subsection if and only if the following conditions exist:

(i) the receipt of property or reduction of claim, which would have given rise to the obligation to account if such Trustee had continued as Trustee, occurred after the beginning of such 4 month period; and

(ii) such receipt of property or reduction of claim occurred within 4 months after such resignation or removal.

(b) There shall be excluded from the operation of Subsection (a) of this Section a creditor relationship arising from

(1) the ownership or acquisition of securities issued under any indenture, or any security or securities having a maturity of one year or more at the time of acquisition by the Trustee;

(2) advances authorized by a receivership or bankruptcy court of competent jurisdiction, or by this Indenture, for the purpose of preserving any property which shall at any time be subject to the lien of this Indenture or of discharging tax liens or other prior liens or encumbrances thereon, if notice of such advances and of the circumstances surrounding the making thereof is given to the Securityholders at the time and in the manner provided in this Indenture;

(3) disbursements made in the ordinary course of business in the capacity of trustee under an indenture, transfer agent, registrar, custodian, paying agent, fiscal agent or depositary, or other similar capacity;

(4) an indebtedness created as a result of services rendered or premises rented; or an indebtedness created as a result of goods or securities sold in a cash transaction as defined in Subsection (c) of this Section;

(5) the ownership of stock or of other securities of a corporation organized under the provisions of Section 25(a) of the Federal Reserve Act, as amended, which is directly or indirectly a creditor of APS; or

(6) the acquisition, ownership, acceptance or negotiation of any drafts, bills of exchange, acceptances or obligations which fall within the classification of self-liquidating paper as defined in Subsection (c) of this Section.

(c) For the purposes of this Section only:

(1) The term "*default*" means any failure to make payment in full of the principal of or interest on any of the Securities or upon the other indenture securities when and as such principal or interest becomes due and payable;

(2) The term "*other indenture securities*" means securities upon which the Person obligated thereunder is an obligor (as defined in the Trust Indenture Act) outstanding under any other indenture (i) under which the Trustee is also trustee, (ii) which contains provisions substantially similar to the provisions of this Section, and (iii) under which a default exists at the time of the apportionment of the funds and property held in a special account as provided in Subsection (a) of this Section;

(3) The term "*cash transaction*" means any transaction in which full payment for goods or securities sold is made within 7 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;

(4) The term "*self-liquidating paper*" means any draft, bill of exchange, acceptance or obligation which is made, drawn, negotiated or incurred by any obligor on the Securities 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 such obligor arising from the making, drawing, negotiating or incurring of the draft, bill of exchange, acceptance or obligation;

(5) The term "*obligor*" means any obligor upon the Securities within the meaning of the TIA.

SECTION 9.14. *Maintenance of Agencies.*

(a) There shall at all times be maintained in the Borough of Manhattan, the City of New York, an office or agency where Securities may be presented or surrendered for transfer or exchange or for the registration thereof, and for payment of principal, premium (if any) and interest and where notices and demands to or upon the Trustee in respect of the Securities or of this Indenture may be served. Such office or agency shall be initially at the Paying Agent's Office. Written notice of the location of each such other office or agency and of any change of location thereof shall be given to the Company and to the Trustee. In the event that no such office or agency shall be maintained or no such notice of location or of change of location shall be given, presentations and demands may be made and notices may be served at the Corporate Trust Office.

(b) There shall at all times be a Security Registrar and a Paying Agent hereunder. Each such Authorized Agent shall be a bank or trust company, shall be a corporation organized and doing business under the laws of the United States or any State thereof, with a combined capital and surplus of at least \$50,000,000, and shall be authorized under such laws to exercise corporate trust powers, subject to supervision by Federal or State authorities. Chemical Bank, at its office specified in the first paragraph of this Indenture, is hereby appointed as Paying Agent and Security Registrar hereunder.

(c) Any Paying Agent (other than the Trustee) from time to time appointed hereunder shall execute and deliver to the Trustee an instrument in which said Paying Agent shall agree with the Trustee, subject to the provisions of this Section, that such Paying Agent will

(1) hold all sums held by it for the payment of principal of, and premium (if any) and interest on 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;

(2) give the Trustee within five days thereafter notice of any default by any obligor upon the Securities in the making of any such payment of principal, premium (if any) or interest; and

(3) at any time during the continuance of any such default, upon the written request of the Trustee, forthwith pay to the Trustee all sums so held in trust by such Paying Agent.

Notwithstanding any other provision of this Indenture, any payment required to be made to or received or held by the Trustee may, to the extent authorized by written instructions of the Trustee, be made to or received or held by a Paying Agent in the Borough of Manhattan, the City of New York, for the account of the Trustee.

(d) Any corporation into which any Authorized Agent may be merged or converted or with which it may be consolidated, or any corporation resulting from any merger, consolidation or conversion to which any Authorized Agent shall be a party, or any corporation succeeding to the corporate trust business of any Authorized Agent, shall be the successor of such Authorized Agent hereunder, if such successor corporation is otherwise eligible under this Section, without the execution or filing of any paper or any further act on the part of the parties hereto or such Authorized Agent or such successor corporation.

(e) Any Authorized Agent may at any time resign by giving written notice of resignation to the Trustee, APS and the Company. The Company may, and at the request of the Trustee or any Lessor shall, at any time, terminate the agency of any Authorized Agent by giving written notice of termination to such Authorized Agent and to the Trustee. Upon the resignation or termination of an Authorized Agent or in case at any time any such Authorized Agent shall cease to be eligible under this Section (when, in either case, no other Authorized Agent performing the functions of such Authorized Agent shall have been appointed), the Company shall promptly appoint one or more qualified successor Authorized Agents approved by the Trustee and each Lessor to perform the functions of the Authorized Agent which has resigned or whose agency has been terminated or who shall have ceased to be eligible under this Section. The Company shall give written notice of any such appointment to all Holders as their names and addresses appear on the Security Register.

ARTICLE TEN

SECURITYHOLDERS' LISTS AND REPORTS
BY TRUSTEE AND APSSECTION 10.01. *APS to Furnish Trustee Names and Addresses of Securityholders.*

APS will furnish or cause to be furnished to the Trustee semiannually, between January 15 and January 30, inclusive, and between July 15 and July 30, inclusive, in each year, and at such other times as the Trustee may request in writing, within 30 days after receipt by APS of any such request, a list, in such form as the Trustee may reasonably require, of the names and addresses of the Holders of Securities, in each case as of a date not more than 15 days prior to the time such list is furnished; provided, however, that so long as the Trustee is the sole Security Registrar, no such list need be furnished for so long as a copy of the Security Register is being furnished to the Trustee pursuant to Section 9.14(b).

SECTION 10.02. *Preservation of Information; Communications to Securityholders.*

(a) The Trustee shall preserve, in as current a form as is reasonably practicable, the names and addresses of Holders of Securities contained in the most recent list furnished to the Trustee as provided in Section 9.14(b) or Section 10.01, as the case may be, and the names and addresses of Holders of Securities received by the Trustee in its capacity as Security Registrar, if so acting. The Trustee may destroy any list furnished to it as provided in Section 9.14(b) or Section 10.01, as the case may be, upon receipt of a new list so furnished.

(b) If three or more Holders of Securities (hereinafter referred to as "applicants") apply in writing to the Trustee, and furnish to the Trustee reasonable proof that each such applicant has owned a Security for a period of at least six months preceding the date of such application, and such application states that the applicants desire to communicate with other Holders of Securities with respect to their rights under this Indenture or under the Securities and is accompanied by a copy of the form of proxy or other communication which such applicants propose to transmit, then the Trustee shall, within 5 Business Days after the receipt of such application, at its election, either:

(i) afford such applicants access to the information preserved at the time by the Trustee in accordance with Section 10.02(a), or

(ii) inform such applicants as to the approximate number of Holders of Securities whose names and addresses appear in the information preserved at the time by the Trustee in accordance with Section 10.02(a), and as to the approximate cost of mailing to such Securityholders the form of proxy or other communication, if any, specified in such application.

If the Trustee shall elect not to afford such applicants access to such information, the Trustee shall, upon the written request of such applicants, mail to each Securityholder whose name and address appear in the information preserved at the time by the Trustee in accordance with Section 10.02(a), a copy of the form of proxy or other communication which is specified in such request, with reasonable promptness after a tender to the Trustee of the material to be mailed and of payment, or provision for the payment, of the reasonable expenses of mailing, unless within five days after such tender, the Trustee shall mail to such applicants and file with the Commission, together with a copy of the material to be mailed, a written statement to the effect that, in the opinion of the Trustee, such mailing would be contrary to the best interests of the Holders of Securities or would be in violation of applicable law. Such written statement shall specify the basis of such opinions. If the Commission, after opportunity for a hearing upon the objections specified in the written statement so filed, shall enter an order refusing to sustain any of such objections or if, after the entry of an order sustaining one or more of such objections, the Commission shall find, after notice and opportunity for hearing, that all the objections so sustained have been met and shall enter an order so declaring, the Trustee shall mail copies of such material to all such Securityholders with reasonable promptness after the entry of such order and the renewal of such tender; otherwise the Trustee shall be relieved of any obligation or duty to such applicants respecting their application.

(c) Every Holder of Securities, by receiving and holding the same, agrees with APS and the Trustee that neither APS nor the Trustee shall be held accountable by reason of the disclosure of any such information as to the names and addresses of the Holders of Securities in accordance with Section 10.02(b), regardless of the source from which such information was derived, and that the Trustee shall not be held accountable by reason of mailing any material pursuant to a request made under Section 10.02(b).

SECTION 10.03. *Reports by Trustee.*

(a) Within 60 days after May 15 in each year, commencing with 1987, the Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, a brief report dated as of such May 15 with respect to:

(1) its eligibility under Section 9.09 and its qualifications under Section 9.08, or in lieu thereof, if to the best of its knowledge it has continued to be eligible and qualified under said Sections, a written statement to such effect;

(2) the character and amount of any advances (and if the Trustee elects so to state, the circumstances surrounding the making thereof) made by the Trustee (as such) which remain unpaid on the date of such report, and for the reimbursement of which it claims or may claim a lien or charge, prior to that of the Securities, on any property or funds held or collected by it as Trustee, except that the Trustee shall not be required (but may elect) to report such advances if such advances so remaining unpaid aggregate not more than $\frac{1}{2}$ of 1% of the principal amount of the Securities Outstanding on the date of such report;

(3) the amount, interest rate and maturity date of all other indebtedness owing by an obligor on the Securities within the meaning of the TIA to the Trustee in its individual capacity, on the date of such report, with a brief description of any property held as collateral security therefor, except an indebtedness based upon a creditor relationship arising in any manner described in Section 9.13(b) (2), (3), (4) or (6);

(4) the property and funds, if any, physically in the possession of the Trustee as such on the date of such report;

(5) any release, or release and substitution, of property subject to the lien of this Indenture (and the consideration therefor, if any) which the Trustee has not previously reported;

(6) any additional issue of Securities which the Trustee has not previously reported; and

(7) any action taken by the Trustee in the performance of its duties hereunder which it has not previously reported and which in its opinion materially affects the Securities, except action in respect of a

default, notice of which has been or is to be withheld by the Trustee in accordance with Section 9.02.

(b) The Trustee shall transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, a brief report with respect to:

(1) the release, or release and substitution, of property subject to the Lien of this Indenture (and the consideration therefor, if any), such report to be transmitted within 90 days of such time; and

(2) the character and amount of any advances (and if the Trustee elects so to state, the circumstances surrounding the making thereof) made by the Trustee (as such) since the date of the last report transmitted pursuant to Subsection (a) of this Section (or if no such report has yet been so transmitted, since the date of execution of this instrument) for the reimbursement of which it claims or may claim a lien or charge, prior to that of the Securities, on property or funds held or collected by it as Trustee, and which it has not previously reported pursuant to this Subsection, except that the Trustee shall not be required (but may elect) to report such advances if such advances remaining unpaid at any time aggregate 10% or less of the principal amount of the Securities Outstanding at such time, such report to be transmitted within 90 days after such time.

(c) A copy of each such report shall, at the time of such transmission to Securityholders, be filed by the Trustee with each stock exchange upon which the Securities are listed, and also with the Commission. APS will notify the Trustee when the Securities are listed on any stock exchange.

SECTION 10.04. Reports by APS.

APS will

(1) file with the Trustee, within 15 days after APS is required to file the same with the Commission, copies of the annual reports and of the information, documents and other reports (or copies of such portions of any of the foregoing as the Commission may from time to time by rules and regulations prescribe) which APS may be required to file with the Commission pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934; or, if APS is not required to file information, documents or reports pursuant to either of said Sections, then it will file with the Trustee and the Commission, in accordance

with rules and regulations prescribed from time to time by the Commission, such of the supplementary and periodic information, documents and reports which may be required pursuant to Section 13 of the Securities Exchange Act of 1934 in respect of a security listed and registered on a national securities exchange as may be prescribed from time to time in such rules and regulations;

(2) file with the Trustee and the Commission, in accordance with rules and regulations prescribed from time to time by the Commission, such additional information, documents and reports with respect to compliance by APS with the conditions and covenants of this Indenture as may be required from time to time by such rules and regulations; and

(3) transmit by mail to all Securityholders, as their names and addresses appear in the Security Register, within 30 days after the filing thereof with the Trustee, such summaries of any information, documents and reports required to be filed by APS pursuant to paragraphs (1) and (2) of this Section as may be required by rules and regulations prescribed from time to time by the Commission.

ARTICLE ELEVEN

SUPPLEMENTAL INDENTURES

SECTION 11.01. *Supplemental Indentures Without Consent of Securityholders.*

Without the consent of the Holders of any Securities, APS, when authorized by a Board Resolution, the Company and the Trustee, at any time and from time to time, may enter into one or more indentures supplemental hereto (a "*Series Supplemental Indenture*" in the case of item 1 below), in form satisfactory to the Trustee, for any of the following purposes:

(1) to establish the form and terms of Securities of any series of Securities permitted by Sections 2.01 and 2.03; or

(2) to evidence the succession of another corporation to APS, and the assumption by any such successor of the covenants of APS herein contained, or to evidence the succession of another corporation to the

Company, and the assumption by any such successor of the covenants of the Company herein and in the Securities contained; or

(3) to add to the covenants of APS or the Company, for the benefit of the Holders of the Securities, or to surrender any right or power herein conferred upon APS or the Company; or

(4) to convey, transfer and assign to the Trustee, and to subject to the Lien of this Indenture, with the same force and effect as though included in the Granting Clauses hereof, additional Pledged Lessor Notes or additional properties or assets, and to correct or amplify the description of any property at any time subject to the Lien of this Indenture or to assure, convey and confirm unto the Trustee any property subject or required to be subject to the Lien of this Indenture; or

(5) to modify, eliminate or add to the provisions of this Indenture to such extent as shall be necessary to continue the qualification of this Indenture (including any supplemental indenture) under the TIA, or under any similar federal statute hereafter enacted, and to add to this Indenture such other provisions as may be expressly permitted by the TIA, excluding, however, the provisions referred to in Section 316(a)(2) of the TIA as in effect at the date as of which this instrument was executed or any corresponding provision in any similar federal statute hereafter enacted; or

(6) 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 provisions with respect to matters or questions arising under this Indenture, provided such action shall not adversely affect the interest of the Holders of the Securities.

SECTION 11.02. *Supplemental Indenture With Consent of Securityholders.*

With the consent of (i) the Holders of not less than a majority in principal amount of the Outstanding Securities, by Act of said Holders delivered to the Company and the Trustee, and (ii) APS, when authorized by a Board Resolution, and the Company may, and the Trustee, subject to Section 11.03, shall, enter into an indenture or indentures supplemental hereto for the purpose of adding any provisions to or changing in any manner the rights and obligations of the Holders of the Securities and of APS and the Company under this Indenture; *provided, however*, that no such supplemental indenture shall, without the consent of the Holder of each Outstanding Security affected thereby,

(1) change the Stated Maturity of the principal of, or any installment of interest on, or the dates or circumstances of payment of premium (if any) on, any Security, or reduce the principal amount thereof or the interest thereon or any premium payable upon the redemption thereof, or change the place of payment where, or the coin or currency in which, any Security or the premium (if any) or the interest thereon is payable, or impair the right to institute suit for the enforcement of any such payment of principal or interest on or after the Stated Maturity thereof (or, in the case of redemption, on or after the Redemption Date) or such payment of premium (if any) on or after the date such premium becomes due and payable or change the dates or the amounts of payments to be made through the operation of the Sinking Fund in respect of such Securities, or

(2) permit the creation of any lien prior to or, except with respect to additional series of Securities issued in accordance with the terms of this Indenture, *pari passu* with the Lien of this Indenture with respect to any of the Pledged Property, or terminate the Lien of this Indenture on any Pledged Property (except in each case as permitted by, and pursuant to, Article Four) or deprive any Securityholder of the security afforded by the Lien of this Indenture, or

(3) reduce the percentage in principal amount of the Outstanding Securities, the consent of whose Holders is required for any such supplemental indenture, or the consent of whose Holders is required for any waiver (of compliance with certain provisions of this Indenture or certain defaults hereunder and their consequences) provided for in this Indenture, or

(4) modify any of the provisions of this Section or Section 8.08, except to increase any such percentage or to provide that certain other provisions of this Indenture cannot be modified or waived without the consent of the Holder of each Security affected thereby.

Upon receipt by the Trustee of Board Resolutions of APS and the Company and such other documentation as the Trustee may reasonably require and upon the filing with the Trustee of evidence of the Act of said Holders, the Trustee shall join in the execution of such supplemental indenture or other instrument, as the case may be, subject to the provisions of Sections 11.03 and 11.04.

It shall not be necessary for any Act of Securityholders 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.

SECTION 11.03. *Documents Affecting Immunity or Indemnity.*

If in the opinion of the Company or the Trustee any document required to be executed by it pursuant to the terms of Section 11.02 affects any interest, right, duty, immunity or indemnity in favor of the Company or the Trustee under this Indenture or any of the Participation Agreements, the Company or the Trustee, as the case may be, may in its discretion decline to execute such document.

SECTION 11.04. *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 receive, and (subject to Section 9.01) 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.

SECTION 11.05. *Effect of Supplemental Indentures.*

Upon the execution 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.

SECTION 11.06. *Conformity with Trust Indenture Act.*

Every supplemental indenture executed pursuant to this Article shall conform to the requirements of the TIA as then in effect.

SECTION 11.07. *Reference in Securities to Supplemental Indentures.*

Securities authenticated and delivered after the execution of any supplemental indenture pursuant to this Article may, and shall if required by any Lessor or the Company, bear a notation in form approved by such Lessor, the Company and the Trustee as to any matter provided for in such supplemental indenture; and, in such case, suitable notation may be made upon Outstanding Securities after proper presentation and demand. If any Lessor or the Company shall so determine, new Securities so modified as to

conform, in the opinion of such Lessor, the Company and the Trustee, 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.

ARTICLE TWELVE

DEFEASANCE

SECTION 12.01. *Payment of Indebtedness; Satisfaction and Discharge of this Indenture.*

This Indenture shall cease to be of further effect (except as to any rights of registration of transfer or exchange of Securities herein expressly provided for and the rights of the Trustee, any predecessor Trustee and any Authorized Agent under Section 9.07), and the Trustee, on demand and at the expense of the Company, shall execute proper instruments acknowledging satisfaction and discharge of this Indenture, when

(1) either

(A) all Securities theretofore authenticated and delivered (other than (i) Securities which have been destroyed, lost or stolen and which have been replaced or redeemed as provided in Section 2.09 and (ii) Securities for the payment of which money held in trust hereunder has been paid to the Company and discharged from such trust, as provided in Section 5.03) have been delivered to the Trustee for cancellation; or

(B) all such Securities not theretofore delivered to the Trustee for cancellation

(i) have become due and payable, or

(ii) will become due and payable at their Stated Maturity of principal within one year, or

(iii) are to be called for redemption within one year under arrangements satisfactory to the Trustee for the giving of notice of redemption by the Trustee in the name and at the expense of the Company, and the Company, in the case of (i), (ii) or (iii) above, has deposited or caused to be deposited with the Trustee in trust (subject to Section 9.06 hereof) for the purpose of paying and discharging the entire indebted-

ness on such Securities not theretofore cancelled by the Trustee or delivered to the Trustee for cancellation, an amount sufficient to discharge such indebtedness, including principal, premium (if any) and interest to the date of such deposit (in the case of Securities which have become due and payable), or to the Stated Maturity of principal or Redemption Date, as the case may be;

(2) All other sums then due and payable hereunder have been paid; and

(3) APS or the Company has delivered to the Trustee an Officers' Certificate and an Opinion of Counsel each stating that all conditions precedent herein provided for relating to the satisfaction and discharge of this Indenture have been complied with.

SECTION 12.02. *Application of Deposited Money:*

All money deposited with the Trustee pursuant to Section 12.01 shall be held in trust and applied by it, in accordance with the provisions of the Securities and this Indenture, to the payment to the Persons entitled thereto of the principal, premium (if any), and interest for the payment of which such money has been deposited with the Trustee.

ARTICLE THIRTEEN

**RELEASE OF FUNDS BY THE TRUSTEE
FOR PAYMENT OF THE PLEDGED LESSOR
NOTES AND RELEASE AND SUBSTITUTION
OF PLEDGED PROPERTY**

SECTION 13.01. *Conditions Precedent to Release of Funds by the Trustee for Payment of the Pledged Lessor Notes.*

The obligation of the Trustee to make payments to the Lessors pursuant to Section 2.15(b) hereof is subject to the receipt by the Trustee of the following:

(a) an executed counterpart of a supplemental indenture appropriate to subject to the Lien of this Indenture the related Pledged Lessor Notes;

(b) the documents, opinions and certificates specified in the proviso to Section 2.04;

(c) a certificate of each Lessor dated as of the Closing Date under the related Participation Agreement (i) specifying the principal amount of the Pledged Lessor Note to be issued thereby and (ii) stating that (A) such Lessor has received the amount of the Equity Participant's investment pursuant to applicable provisions of such Participation Agreement and that such amount is available for use by such Lessor pursuant to applicable provisions of such Participation Agreement upon receipt of the amount to be paid by the Trustee with respect to such Pledged Lessor Note pursuant to Section 2.15(b) hereof; (B) to the best knowledge of such Lessor no event has occurred and is continuing which constitutes an Indenture Event of Default, or would constitute an Indenture Event of Default after notice or lapse of time or both under the related Lease Indenture and (C) the Pledged Lessor Note of such Lessor has been duly authorized, executed and delivered by such Lessor and is a valid and binding obligation of such Lessor; and

(d) such other documents and evidence with respect to the Lessors and the Company as the Trustee may reasonably request.

This instrument may be executed in any number of counterparts, each of which when so executed shall be deemed to be an original, but all such counterparts shall together constitute but one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this Indenture to be duly executed, and their respective corporate seals to be hereunto affixed and attested, all as of the day and year first above written.

PVNGS FUNDING CORP., INC.

By /s/ PETER FARLEY
Vice President

Attest:

/s/ RICHARD FRANZEN
Assistant Secretary

ARIZONA PUBLIC SERVICE COMPANY

By /s/ P. A. WILLIAMS
Vice President and Treasurer

Attest:

/s/ FAYE WIDENMANN
Secretary

CHEMICAL BANK

By /s/ T. J. FOLEY
Vice President

Attest:

/s/ G. MCFARLANE
Trust Officer

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On this 19th day of November, 1986, before me personally came Peter C. Farley, to me known, who, being by me duly sworn, did depose and say that he resides at Wilmington, Delaware; that he is the Vice President of PVNGS FUNDING CORP., INC., one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693465
Qualified in New York County
Commission Expires March 30, 1987

[NOTARIAL SEAL]

STATE OF NEW YORK }
 COUNTY OF NEW YORK } ss.:

On this 19th day of November, 1986, before me personally came Paul A. Williams II, to me known, who, being by me duly sworn, did depose and say that he resides at Phoenix, Arizona; that he is the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
 Notary Public, State of New York
 No. 31-4693168
 Qualified in New York County
 Commission Expires March 30 1987

[NOTARIAL SEAL]

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On the 19th day of November, 1986, before me personally came T. J. Foley, to me known who, being by me duly sworn, did depose and say that he resides at Bethpage, New York; that he is a Vice-President of CHEMICAL BANK, a New York banking corporation and one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation, and that he signed his name thereto on behalf of said corporation by like order.

/s/ DAVID A. SPIVAK

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693466
Qualified in New York County
Commission Expires March 30, 1987

[NOTARIAL SEAL]

EXHIBIT A
TO
COLLATERAL TRUST INDENTURE
REQUIREMENTS FOR PLEDGED LESSOR
NOTES AND LEASE INDENTURES

The Pledged Lessor Notes and the Lease Indentures relating to any series of Securities shall contain the provisions summarized below or other provisions substantially as protective or more protective of the interests of Holders of Outstanding Securities. Notwithstanding the foregoing, (i) the Principal Instruments in connection with the initial series of Securities issued under this Indenture shall be deemed to satisfy all criteria set forth in this Exhibit A and (ii) the Principal Instruments in connection with any subsequent series of Securities, if substantially similar in form and substance to the Principal Instruments in connection with such initial series of Securities, shall also be deemed to satisfy all criteria set forth in this Exhibit A.

I. Each Pledged Lessor Note will:

(i) be duly issued pursuant to, and be secured by, the related Lease Indenture;

(ii) provide for the payment to the registered holder thereof, not later than when due, of amounts at least equal to that portion of all principal of and premium, if any, and interest on the series of Securities issued in connection with and relating to the pledge thereof under the Indenture, such payment to be without defenses or set-offs and otherwise unconditional;

(iii) (A) if such Pledged Lessor Note is the initial series issued under the related Lease Indenture, the principal amount thereof shall not exceed an amount equal to 80% of the sum of the aggregate purchase price of the property being purchased with the proceeds of the issuance and sale of such Lessor Note; and (B) if such Pledged Lessor Note is of an additional series issued under the related Lease Indenture, the sum of the principal amount thereof and the principal amount of Pledged Lessor Notes theretofore issued under such Lease Indenture shall not exceed an amount equal to 80% of the sum of (1)

the aggregate purchase price of property being purchased with the proceeds of the issuance and sale of such Lessor Note and (2) the aggregate purchase price of the property purchased with the proceeds of the issuance and sale of each Pledged Lessor Note theretofore issued; and

(iv) provide that no Change to the Pledged Lessor Note may be made without the consent of the holder thereof.

II. Each Lease Indenture will:

(i) assign to the Lease Indenture Trustee obligations under the related Lease to which the Owner Trustee then or thereafter is entitled at least sufficient to pay the principal of, premium, if any, and interest on the related Pledged Lessor Note; and

(ii) contain provisions no less protective of the interests of Holders of Securities than the following provisions of the Lease Indentures in connection with the initial series of Securities: Article II, Sections 3.4, 3.5, 3.6, 3.8, 3.11, Article V, Article VI and Article VII.

PVNGS FUNDING CORP., INC.,

ARIZONA PUBLIC SERVICE COMPANY

and

CHEMICAL BANK,
as Trustee

SERIES 1986 BOND SUPPLEMENTAL INDENTURE

dated as of November 15, 1986

to

COLLATERAL TRUST INDENTURE

dated as of November 1, 1986

Providing for the Issuance of
\$273,000,000 Aggregate Principal Amount
of Secured Lease Obligation Bonds, Series 1986
with the Interest Rates and Stated Maturities
Set Forth Herein

PALO VERDE NUCLEAR GENERATING STATION

WHEREAS, the Bonds to be issued hereunder are to be substantially in the form annexed as Schedule 1 hereto; and

WHEREAS, all acts and things necessary to make the Bonds, when executed by the Company and authenticated and delivered by the Trustee as provided in the Original Indenture, the valid, binding and legal obligations of the Company, and to constitute these presents a valid and binding supplemental indenture and agreement according to its terms, have been done and performed, and the execution of this Series 1986 Bond Supplemental Indenture and the creation and issuance under the Indenture of \$273,000,000 aggregate principal amount of the Bonds have in all respects been duly authorized, and the Company, in the exercise of legal right and power in it vested, executes this Series 1986 Bond Supplemental Indenture and proposes to create, execute, issue and deliver the Bonds:

NOW, THEREFORE, THIS SERIES 1986 BOND SUPPLEMENTAL INDENTURE WITNESSETH:

That in order to establish the form and terms of and to authorize the authentication and delivery of the Bonds, and in consideration of the acceptance of the Bonds by the holders thereof and of the sum of one dollar duly paid to the Company by the Trustee at the execution of these presents, the receipt whereof is hereby acknowledged, the Company and APS each covenant and agree with the Trustee, for the equal and proportionate benefit of the respective holders from time to time of the Bonds, as follows:

ARTICLE ONE

THE BONDS

SECTION 1.01. Terms of the Bonds.

There is hereby created a series of Securities designated "Secured Lease Obligation Bonds, Series 1986". Bonds in the aggregate principal amount of \$273,000,000 may forthwith be executed by the Company and delivered to the Trustee for authentication and delivery by the Trustee in accordance with the provisions of Section 2.04 of the Original Indenture in the following amounts for the Stated Maturities of principal and at the interest rates indicated:

<u>Stated Maturity of Principal</u>	<u>Interest Rate</u>	<u>Principal Amount</u>
December 30, 1998	9%	\$ 35,184,000
June 30, 2015	10.45%	237,816,000
		<hr/> \$273,000,000

The Bonds shall be payable, bear interest and have and be subject to such other terms as provided in the form of Bond attached as Schedule 1 hereto.

SECTION 1.02. Mandatory Redemption of the Bonds.

(a) Termination of Lease. In the event that there shall occur under Section 14 of any Lease identified in Schedule 2 hereto a termination of such Lease, Bonds shall be redeemed, in part, in proportion to the principal amount of the Pledged Lessor Notes related to such Lease (the Prepaid Lessor Notes) prepaid in accordance with their terms and Section 5.2 of the Lease Indenture under which such Pledged Lessor Notes are issued. Any such redemption shall be on the date set

forth in the redemption notice delivered by the Trustee pursuant to Section 1.02(b) of this Series 1986 Bond Supplemental Indenture and shall be made to the extent that the Prepaid Lessor Notes are so prepaid, together with accrued interest thereon.

(b) Notice of Redemption and Redemption Date. Redemption of Bonds pursuant to Section 1.02(a) of this Series 1986 Bond Supplemental Indenture shall be on the Redemption Date set forth in the redemption notice delivered by the Trustee pursuant to Section 6.03 of the Original Indenture, which Redemption Date shall correspond to the Obsolescence Redemption Date following the Termination Date specified in the Termination Notice received by the Trustee relating to the Prepaid Lessor Notes.

(c) Selection. Any Bonds redeemed pursuant to Section 1.02(a) of this Series 1986 Bond Supplemental Indenture shall be selected in accordance with Section 6.02 of the Original Indenture, but without giving effect to the proviso contained in such Section.

(d) Redemption Price. The Redemption Price for any Bond to be redeemed pursuant to this Section 1.02 shall be 100% of the principal amount thereof, together with accrued interest to the Redemption Date.

SECTION 1.03. Optional Redemption of Bonds.

The Bonds shall be redeemable prior to maturity at the option of the Company at the times and redemption prices set forth in the form of Bond attached as Schedule 1 hereto.

SECTION 1.04. Sinking Fund.

(a) Amounts and Dates. The Bonds shall be redeemed through operation of a sinking fund. The amount of each Sinking Fund payment (subject to adjustment as provided in paragraph (b) below) and each

Sinking Fund Date applicable to a Stated Maturity of principal of the Bonds are as set forth below:

Sinking Fund Date	Stated Maturity	
	December 30, 1998	June 30, 2015
December 30, 1989	\$ 65,000	-
June 30, 1990	495,000	-
December 30, 1990	978,000	-
June 30, 1991	1,022,000	-
December 30, 1991	1,068,000	-
June 30, 1992	1,116,000	-
December 30, 1992	1,166,000	-
June 30, 1993	1,218,000	-
December 30, 1993	1,273,000	-
June 30, 1994	1,330,000	-
December 30, 1994	1,391,000	-
June 30, 1995	1,454,000	-
December 30, 1995	1,518,000	-
June 30, 1996	1,587,000	-
December 30, 1996	1,658,000	-
June 30, 1997	1,733,000	-
December 30, 1997	5,136,000	-
June 30, 1998	5,367,000	-
December 30, 1998	5,609,000	-
June 30, 1999		\$ 3,485,000
December 30, 1999		4,722,000
June 30, 2000		5,169,000
December 30, 2000		5,148,000
June 30, 2001		5,147,000
December 30, 2001		4,558,000
June 30, 2002		4,979,000
December 30, 2002		4,862,000
June 30, 2003		5,313,000
December 30, 2003		5,187,000
June 30, 2004		5,533,000
December 30, 2004		5,392,000
June 30, 2005		5,856,000
December 30, 2005		5,704,000
June 30, 2006		6,250,000

Sinking Fund Date	Stated Maturity	
	December 30, 1998	June 30, 2015
December 30, 2006		6,086,000
June 30, 2007		6,670,000
December 30, 2007		6,493,000
June 30, 2008		7,118,000
December 30, 2008		6,928,000
June 30, 2009		7,596,000
December 30, 2009		7,393,000
June 30, 2010		8,107,000
December 30, 2010		7,888,000
June 30, 2011		8,652,000
December 30, 2011		8,417,000
June 30, 2012		9,234,000
December 30, 2012		10,279,000
June 30, 2013		9,751,000
December 30, 2013		11,616,000
June 30, 2014		14,316,000
December 30, 2014		17,035,000
June 30, 2015		6,932,000

(b) Certain Adjustments to Sinking Funds.

The principal amount of Bonds of a particular Stated Maturity of principal to be redeemed through operation of the Sinking Fund for the Bonds of such Stated Maturity of principal may be adjusted once (upward or downward) at the discretion of the Company (contemporaneously with similar adjustments for all Stated Maturities of principal) prior to June 30, 1989; provided, however, that no such adjustment shall be made by the Company which will increase or reduce the average life of the Bonds of such Stated Maturity of principal (calculated in accordance with generally accepted financial practice) from the date of initial issuance by more than 6 months; provided further, however, such adjustment may only be made in connection with an adjustment to basic rent pursuant to Section 3(d) of one or more of the Leases identified in Schedule 2 hereto. If the Company shall elect to make the foregoing adjustment, the Company shall deliver to the Trustee and APS at

least 60 days prior to the first Sinking Fund Date proposed to be affected by such adjustment, a Company Request (w) stating that the Company has elected to make such adjustment in connection with adjustments to basic rent under one or more of such Leases, (x) setting forth a revised schedule of principal amounts of the Sinking Fund applicable to Bonds of the affected Stated Maturity of principal, (y) attaching a copy of the revised schedules of principal amortization for the related Pledged Lessor Notes identified in Schedule 2 hereto, and (z) attaching calculations showing that (i) the average life of the Bonds of the affected Stated Maturity of principal will not be reduced or increased except as permitted by this paragraph (b), (ii) the aggregate principal amount of the Pledged Lessor Notes identified on Schedule 2 hereto equals the aggregate principal amount of the Bonds and (iii) the aggregate amortization of the principal amount of such Pledged Lessor Notes is sufficient to repay in full, as and when due, the principal amount of the Bonds as and when due, whether upon redemption through operation of the applicable Sinking Funds or at maturity. The Trustee may rely on such Company Request and shall have no duty with respect to the calculations referred to in the foregoing clause (z), other than to make them available for inspection by any Holder of Bonds at the Corporate Trust Office upon reasonable notice. The Trustee shall, at the expense of APS, send to each Holder of Bonds of the affected Stated Maturity of principal at least 20 days before the first Sinking Fund Date to be affected thereby, by first class mail, a copy of such revised schedule of principal amounts of Sinking Fund payments applicable to such Bonds.

(c) Redemption Price. The Redemption Price for any Bond to be redeemed pursuant to paragraph (a) of this Section 1.04 shall be 100% of the principal amount thereof, together with accrued interest to the Redemption Date.

ARTICLE TWO

PLEDGE OF LESSOR NOTES

To secure the payment of the principal of, and premium, if any, and interest, on all the Securities from time to time Outstanding under the Indenture, and the performance of the covenants therein and herein contained, the Company by these presents does grant, bargain, sell, release, convey, assign, transfer, mortgage, hypothecate, pledge, confirm and create a security interest in, unto the Trustee, the Lessor Notes identified on Schedule 2 hereto (herein referred to as the Pledged Lessor Notes).

TO HAVE AND TO HOLD the aforesaid Pledged Lessor Notes unto the Trustee and its successors and assigns forever, in trust and for the uses and purposes and subject to the covenants and conditions set forth in the Indenture.

ARTICLE THREE

MISCELLANEOUS

SECTION 3.01. Execution as Supplemental Indenture.

This Series 1986 Bond Supplemental Indenture is executed and shall be construed as an indenture supplemental to the Original Indenture and, as provided in the Original Indenture, this Series 1986 Bond Supplemental Indenture forms a part thereof. Except as expressly otherwise defined herein or in Schedule 2 hereof, the use of the terms herein is in accordance with the definitions contained in the Original Indenture.

SECTION 3.02. Responsibility for Recitals,
Etc.

The recitals contained herein and in the Bonds, except the Trustee's certificate of authentication, shall be taken as the statements of the Company and APS, and the Trustee assumes no responsibility for the correctness of the same. The Trustee makes no representation as to the validity or sufficiency of this Series 1986 Bond Supplemental Indenture or the Bonds.

SECTION 3.03. Provisions Binding on
Successors.

All the covenants, stipulations, promises and agreements in this Series 1986 Bond Supplemental Indenture contained by or on behalf of the Company shall bind its successors and assigns, whether so expressed or not.

SECTION 3.04. New York Contract.

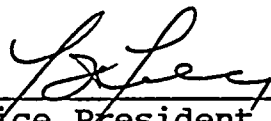
This Series 1986 Bond Supplemental Indenture and each Bond shall be deemed to be a contract under the laws of the State of New York, and for all purposes shall be governed by and construed in accordance with the laws of said state.

SECTION 3.05. Counterparts.

This Series 1986 Bond Supplemental Indenture may be executed in any number of counterparts, each of which shall be an original; but such counterparts shall together constitute but one and the same instrument.

CHEMICAL BANK,
as Trustee

[CORPORATE SEAL]

By 
Vice President

Attest:


Trust Officer

STATE OF NEW YORK)
 : SS.:
COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came Peter C. Farley, to me known, who, being by me duly sworn, did depose and say that he resides at Wilmington, Delaware; that he is the Vice President of PVNGS FUNDING CORP., INC., one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693469
Qualified in New York County
Commission Expires March 30, 1995

STATE OF NEW YORK)
 : SS.:
COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came Paul A. Williams II, to me known, who, being by me duly sworn, did depose and say that he resides at Phoenix, Arizona; that he is the Vice President and Treasurer of ARIZONA PUBLIC SERVICE COMPANY, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-4693463
Qualified in New York County
Commission Expires March 30, 1989

STATE OF NEW YORK)
 : ss.:
COUNTY OF NEW YORK)

On this 19th day of November, 1986, before me personally came T.J. Foley, to me known, who, being by me duly sworn, did depose and say that he resides at Bethpage, New York; that he is Vice President of CHEMICAL BANK, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by authority of the Board of Directors of said corporation, and that he signed his name thereto by like authority.

[NOTARIAL SEAL]

David A. Spivak

DAVID A. SPIVAK
Notary Public, State of New York
No. 31-463463
Qualified in New York County
Commission Expires March 30, 1989

SCHEDULE 1
to
SERIES 1986 BOND
SUPPLEMENTAL INDENTURE

[FORM OF FACE OF BOND]

No. R-

\$ _____

PVNGS FUNDING- CORP., INC.

SECURED LEASE OBLIGATION BOND SERIES 1986

INTEREST RATE	STATED MATURITY	ISSUE DATE	CUSIP
---------------	-----------------	------------	-------

Registered
Holder:

Principal
Amount: Dollars

PVNGS FUNDING CORP., INC., a Delaware corporation (herein called the "Company", which term includes any successor corporation under the Indenture referred to on the reverse hereof), for value received, hereby promises to pay to the Registered Holder hereof, or registered assigns, the Principal Amount (stated above) on the Stated Maturity (stated above) and to pay interest thereon from the date hereof, or from the most recent interest payment date to which interest has been paid or duly provided for, semiannually on June 30 and December 30, in each year, commencing December 30, 1986, at the Interest Rate (stated above) per annum, until the principal hereof is paid in full or made available for payment. The interest so payable, and punctually paid or duly provided for, on any interest payment date will,

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as provided in such Indenture, be paid to the person in whose name this Bond (or one or more Predecessor Securities, as defined in such Indenture) is registered at the close of business on the Regular Record Date (as defined in such Indenture) for such interest, which shall be the June 15 or December 15, as the case may be (whether or not a Business Day, as defined in such Indenture), next preceding such interest payment date. Any such interest not so punctually paid or duly provided for shall forthwith cease to be payable to the Registered Holder on such Regular Record Date, and may be paid to the person in whose name this Bond (or one or more Predecessor Securities) is registered at the close of business on a Special Record Date (as defined in such Indenture) for the payment of such defaulted interest to be fixed by the Trustee, notice of which shall be given to the Bondholders not less than 10 days prior to such Special Record Date, or may be paid at any time in any other lawful manner not inconsistent with the requirements of any securities exchange on which the Bonds may be listed, and upon such notice as may be required by such exchange, all as more fully provided in such Indenture. Payment of the principal of, and premium, if any, and interest on, this Bond will be made at the Corporate Trust Office of the Trustee (or if such office is not in the Borough of Manhattan, The City of New York, at either such office or an office to be maintained in such Borough), in such coin or currency of the United States of America as at the time of payment is legal tender for payment of interest or may be made at the option of the Company by check mailed to the address of the Holder entitled thereto as such address shall appear on the Security Register.

Reference is hereby made to the further provisions of this Bond set forth on the reverse hereof which further provisions shall for all purposes have the same effect as if set forth at this place.

Unless the certificate of authentication hereon has been executed by the Trustee by manual signature, this Bond shall not be entitled to any

[FORM OF REVERSE OF BOND]

PVNGS FUNDING CORP., INC.

SECURED LEASE OBLIGATION BOND, SERIES 1986

This Bond is one of an authorized issue of Securities of the Company known as its "Secured Lease Obligation Bonds, Series 1986" (the "Bonds"). The Bonds are issued under and secured by a Collateral Trust Indenture dated as of November 1, 1986 among the Company, Arizona Public Service Company, an Arizona corporation (herein called "APS"), and Chemical Bank, as Trustee (herein called the "Trustee", which term includes any successor Trustee under the Indenture), as supplemented by the Series 1986 Bond Supplemental Indenture dated as of November 15, 1986 among such parties (collectively, the "Indenture"). All Bonds are secured equally and ratably with one another and with any other Securities of the Company issued under the Indenture, as amended or supplemented. Reference is hereby made to the Indenture for a description of the nature and extent of the securities and other property assigned, pledged and transferred thereunder, the respective rights of the holders of the Bonds and of the Trustee and the Company in respect of such security, and the terms upon which the Bonds are and are to be authenticated and delivered.

The principal of, and premium, if any, and interest on, this Bond are payable from, and secured by, the assets subject to the lien of the Indenture and the income and proceeds received by the Trustee therefrom, and all payments of principal, and premium, if any, and interest shall be made in accordance with the terms of the Indenture.

The Indenture provides that certain nonrecourse promissory notes ("Pledged Lessor Notes") are subject to the lien of the Indenture and that additional Pledged Lessor Notes, as and when issued, can be made subject to the lien of the Indenture pursuant to indenture supplements. The Pledged Lessor Notes subject

to the lien of the Indenture on the date of the initial issuance of Bonds were issued by The First National Bank of Boston, as owner trustee under two separate Trust Agreements with the respective institutional investors named in such Trust Agreements. Such Pledged Lessor Notes were issued under separate documents entitled Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, each between an owner trustee, as lessor, and Chemical Bank, as trustee (each of such Trust Indentures, as it was executed and delivered and as thereafter amended in accordance with its terms, and any similar instruments pursuant to which additional Pledged Lessor Notes are issued, being herein called a "Lease Indenture", each trustee thereunder being herein called a "Lease Indenture Trustee" and each lessor thereunder being herein called a "Lessor"). Reference is made to each Lease Indenture for a description of the nature and extent of property assigned, pledged, transferred and mortgaged thereunder and the rights of the holders of Pledged Lessor Notes. Except as expressly provided in a Lease Indenture, all payments of principal, and premium, if any, and interest to be made on a Pledged Lessor Note issued under such Lease Indenture will be made only from the assets subject to the lien of such Lease Indenture or the income and proceeds received by the Lease Indenture Trustee therefrom, including, in the case of each Lease Indenture, the rights of the Lessor which is a party thereto to receive basic rentals and certain other payments under a Lease with APS relating to an undivided interest in certain assets constituting part of the Palo Verde Nuclear Generating Station (also known as the Arizona Nuclear Power Project) (each of such Leases, as it is executed and delivered and as thereafter amended in accordance with its terms being herein called a "Lease"), which basic rentals and other payments will be at least sufficient to provide for the payment of the principal of, and premium, if any, and interest on, each Pledged Lessor Note issued under such Lease Indenture. Each Holder hereof, by its acceptance of this Bond, agrees (x) that except as expressly provided above, it will look solely to the assets subject to the lien of the Indenture or the income and proceeds received by the

Trustee therefrom, to the extent available for distribution to the Holder hereof as provided in the Indenture and (y) that none of any institutional investor which is a party to a Trust Agreement (an "Equity Participant"), any Lessor, any Lease Indenture Trustee or the Trustee is liable to the Holder hereof or, in the case of an Equity Participant, any Lessor and any Lease Indenture Trustee, to the Trustee for any amounts payable under this Bond or, except as provided in the Indenture with respect to the Trustee, for any liability under the Indenture. An Equity Participant shall not have any duty or responsibility under the Indenture or the Bonds to any Holder or to the Trustee.

The Indenture permits, with certain exceptions as therein provided, the amendment thereof and the modification of the rights and obligations of APS and the Company and the rights of the Holders of the Securities under the Indenture at any time by APS and the Company with the consent of the Holders of not less than a majority in aggregate principal amount of the Securities at the time Outstanding, as defined in the Indenture. The Indenture also contains provisions permitting the Holders of specified percentages in aggregate principal amount of the Securities at the time Outstanding, on behalf of the Holders of all the Securities, to waive compliance by APS and 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 Bond shall be conclusive and binding upon such Holder and upon all future Holders of this Bond and of any Security issued upon the transfer hereof or in exchange herefor or in lieu hereof whether or not notation of such consent or waiver is made upon this Bond.

As provided in the Indenture, the aggregate principal amount of Securities which may be issued thereunder is unlimited. The Bonds are limited in aggregate principal amount to \$273,000,000, consisting of:

<u>Stated Maturity of Principal</u>	<u>Interest Rate</u>	<u>Principal Amount</u>
December 30, 1998	9.00%	\$ 35,184,000
June 30, 2015	10.45%	237,816,000
		<u>\$273,000,000</u>

In the event that one or more Leases are terminated under Section 14 thereof, the Bonds are subject to mandatory redemption in whole or in part in proportion to the principal amount of Pledged Lessor Notes related to such Lease or Leases prepaid in accordance with their terms and Section 5.2 of the Lease Indenture or Lease Indentures under which such Pledged Lessor Notes were issued. Any such redemption shall be on not less than 20 nor more than 60 days' prior notice given as provided in Section 6.03 of the Indenture and Section 1.02(b) of the Series 1986 Bond Supplemental Indenture at a redemption price equal to the principal amount of the Bonds to be redeemed plus accrued interest to the date fixed for redemption, to the extent that the Pledged Lessor Notes relating to the Bonds are prepaid.

The Bonds of each Stated Maturity of principal are also subject to mandatory redemption pursuant to sinking fund installments, as more fully provided in the Indenture, at the principal amount thereof, together with interest accrued to the date fixed for redemption, on the dates and in the respective principal amounts set forth in the Indenture.

The sinking fund installments for the Bonds of a particular Stated Maturity of principal may be adjusted once at the discretion of the Company prior to June 30, 1989, in connection with certain adjustments in basic rent pursuant to any of the Leases.

In the event of any partial redemption of Bonds of a particular Stated Maturity of principal (other than pursuant to the aforementioned sinking fund), the principal amount of Bonds of such Stated Maturity of principal to be redeemed thereafter pursuant to the sinking fund schedule indicated in the Indenture shall be adjusted proportionately as nearly as practicable in accordance with Section 7.01 of the Indenture.

In addition, the Bonds are subject to redemption, in whole or in part, at any time, at the option of the Company, with monies deposited with the Trustee, on not less than 20 nor more than 60 days' notice given as provided in the Indenture, at the following redemption prices (expressed as a percentage of principal amount), together with interest accrued to the date fixed for redemption as follows:

Bonds with a Stated Maturity of principal of December 30, 1998 may be redeemed at the following redemption prices (expressed as a percentage of principal amount), together with interest accrued to the Redemption Date:

<u>If Redeemed During the Twelve Months Beginning December 30,</u>	<u>Redemption Price</u>
1991	104.50%
1992	103.60
1993	102.70
1994	101.80
1995	100.90

and thereafter at the principal amount thereof, together with interest accrued to the Redemption Date; and

Bonds with a Stated Maturity of principal of June 30, 2015 may be redeemed at the following

redemption prices (expressed as a percentage of principal amount), together with interest accrued to the Redemption Date:

<u>If Redeemed During the Twelve Months Beginning December 30,</u>	<u>Redemption Price</u>
1991	107.70%
1992	107.15
1993	106.60
1994	106.05
1995	105.50
1996	104.95
1997	104.40
1998	103.85
1999	103.30
2000	102.75
2001	102.20
2002	101.65
2003	101.10
2004	100.55

and thereafter at the principal amount thereof, together with interest accrued to the Redemption Date.

In the case of any redemption of Bonds, unpaid interest installments whose Stated Maturity, as defined in the Indenture, is on or prior to the date fixed for redemption will be payable to the Holders of such Bonds or one or more Predecessor Securities of record at the close of business on the relevant Regular or Special Record Date referred to on the face hereof.

Bonds (or portions thereof as aforesaid) for which redemption and payment provision is made in accordance with the Indenture shall thereupon cease to be entitled to the lien of the Indenture and shall cease to bear interest from and after the date fixed for redemption.

If an Event of Default, as defined in the Indenture, shall occur, the principal of this Bond may become or be declared due and payable, in the manner and with the effect provided in the Indenture.

This Bond is transferable by the registered owner hereof in person or by attorney authorized in writing, at the corporate trust office of the Bond Registrar, Chemical Bank (or if such office is not in the Borough of Manhattan, The City of New York, at either such office or an office to be maintained in such Borough), upon surrender of this Bond, and upon any such transfer a new Bond of the same Stated Maturity of principal, for the same aggregate principal amount, will be issued to the transferee in exchange herefor.

The Bonds are issuable only as registered Bonds without coupons in denominations of \$1,000 and/or any integral multiple thereof. As provided in, and subject to the provisions of, the Indenture, Bonds of a particular Stated Maturity of principal are exchangeable for other Bonds of such Stated Maturity, but of a different authorized denomination or denominations, as requested by the Holder surrendering the same.

No service charge will be made to any Holder of Bonds for any such transfer or exchange, but the Bond Registrar may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith.

Prior to due presentment for registration of transfer, the person in whose name this Bond is registered shall be deemed to be the owner hereof for the purpose of receiving payment as herein provided and for all other purposes whether or not this Bond be overdue, regardless of any notice to anyone to the contrary.

All capitalized terms used herein, unless defined herein, shall have the meanings ascribed to them in the Indenture.

As provided in the Indenture, the Indenture and the Bonds shall be construed in accordance with and governed by the law of the State of New York.

SCHEDULE 2
to
SERIES 1986 BOND
SUPPLEMENTAL INDENTURE

A. As used in this Series 1986 Bond Supplemental Indenture, the following terms have the following meanings:

(1) Lease Indenture means each of:

(i) the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Indenture Trustee and the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation, as amended by Supplemental Indenture No. 1 thereto, dated as of November 1, 1986; and

(ii) the Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between the Indenture Trustee and the Owner Trustee, as owner trustee for Emerson Capital Corporation, successor to Emerson Finance Co., as amended by Supplemental Indenture No. 1 thereto, dated as of November 1, 1986.

(2) Lessor Note means each of:

(i) the Non-Recourse Promissory Note, Refunding Series (Due December 30, 1998) in the amount of \$14,228,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation to the Company;

(ii) the Non-Recourse Promissory Note, Refunding Series (Due June 30, 2015) in the amount of \$98,772,000 dated

November 19, 1986, payable by the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation to the Company;

(iii) the Non-Recourse Promissory Note, Refunding Series (Due December 30, 1998) in the amount of \$20,956,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Emerson Capital Corporation to the Company; and

(iv) the Non-Recourse Promissory Note, Refunding Series (Due June 30, 2015) in the amount of \$139,044,000 dated November 19, 1986, payable by the Owner Trustee, as owner trustee for Emerson Capital Corporation to the Company.

(3) Lessor or Owner Trustee means The First National Bank of Boston, a national banking association (FNB), in its capacity as owner trustee under two separate Trust Agreements, each dated as of August 1, 1986, with the Equity Participant named therein.

(4) Indenture Trustee means Chemical Bank, a New York banking corporation, as Trustee.

(5) Lease means each of:

(i) the Facility Lease, dated as of August 1, 1986, between APS, as lessee, and the Owner Trustee, as owner trustee for Security Pacific Capital Leasing Corporation, as lessor, as amended by Amendment No. 1 thereto, dated as of November 1, 1986; and

(ii) the Facility Lease, dated as of August 1, 1986, between APS, as lessee, and the Owner Trustee, as owner

trustee for Emerson Capital Corporation, as lessor, as amended by Amendment No. 1 thereto, dated as of November 1, 1986.

(6) Participation Agreement means each of:

(i) the Participation Agreement, dated as of August 1, 1986, among the Equity Participant designated therein, the Company, Bank of America National Trust and Savings Association, for itself and as Agent for the banks named therein, FNB, in its individual capacity and as Owner Trustee for Security Pacific Capital Leasing Corporation, Chemical Bank, in its individual capacity and as Indenture Trustee, and APS, as amended by Amendment No. 1 thereto, dated as of November 1, 1986; and

(ii) the Participation Agreement, dated as of August 1, 1986, among the Equity Participant designated therein, the Company, Bank of America National Trust and Savings Association, for itself and as Agent for the banks named therein, FNB, in its individual capacity and as Owner Trustee for Emerson Capital Corporation, Chemical Bank, in its individual capacity and as Indenture Trustee, and APS, as amended by Amendment No. 1 thereto, dated as of November 1, 1986.

EMERSON CAPITAL CORPORATION

November 19, 1986

CHEMICAL BANK

not in its individual
capacity, but solely as Collateral
Trust Trustee
55 Water Street
New York, New York 10041
Attention: Corporate Trustee Administration

ARIZONA PUBLIC SERVICE COMPANY

PALO VERDE NUCLEAR GENERATING STATION UNIT 2 LEASE

Dear Sirs:

Reference is made to the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among the parties whose signatures appear at the foot hereof. All capitalized terms used herein without definition shall have the meanings set forth in Appendix A to the Participation Agreement.

1. Representations, Warranties and Agreements. Emerson Capital Corporation (assignee of Emerson Finance Co.) (the "Equity Participant"), Bank of America National Trust and Savings Association, for itself and as Agent, PVNGS Funding Corp., Inc., The First National Bank of Boston, as Owner Trustee, Chemical Bank, as Indenture Trustee and APS hereby confirm for your benefit that their respective representations and warranties (in the capacity given therein) and, in the case of APS, agreements, contained in Sections 6, 7, 8, 9, 10, 13 and 14 of the Participation Agreement and, in the case of the Equity Participant, the agreements contained in Section 14(a) of the Participation Agreement, are true and correct and hereby respectively repeat such representations, warranties and, in the case of APS and the Equity Participant,

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agreements to the same extent as if such representations, warranties and agreements were set forth herein in full, whether or not the same are amended after the date hereof.

2. Survival of Representations, Warranties and Agreements. All representations, warranties and agreements contained herein shall survive the execution and delivery of this letter.

3. Successors and Assigns. All terms and provisions of this letter shall inure to your benefit and the benefit of your successors and assigns and each holder from time to time of each Bond.

4. Consequences of Breach. A breach of the representations, warranties and agreements contained herein will not entitle you or any holder of a Bond to exercise remedies or take other action under the Participation Agreement or any other Transaction Document but you may pursue all other rights you have at law or in equity in consequence of such a breach.

5. Governing Law. This letter shall in all respects be governed by, and construed in accordance with, the laws of the State of New York.

6. Execution. This Extension Letter may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall constitute but one and the same instrument. Although this Extension Letter is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Extension Letter shall be effective on the latest of such dates.

EMERSON CAPITAL CORPORATION

By: Val Sharp
President

Date: November 9, 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION
for itself and as Agent for
the Original Loan
Participants

By: _____
Assistant Vice President

By: _____
Title: _____

Date: November , 1986

6. Execution. This Extension Letter may be executed in any number of counterparts and by the different parties hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall constitute but one and the same instrument. Although this Extension Letter is dated as of the date first above written for convenience, the actual dates of execution hereof by the parties hereto are respectively the dates set forth under the signatures hereto, and this Extension Letter shall be effective on the latest of such dates.

EMERSON CAPITAL CORPORATION

By: _____
President

Date: November , 1986

BANK OF AMERICA NATIONAL
TRUST AND SAVINGS
ASSOCIATION
for itself and as Agent for
the Original Loan
Participants

By:  _____
Assistant Vice President

By:  _____
Title: Group Vice President

Date: November 19, 1986

PVNGS FUNDING CORP, INC.

By: [Signature]
Vice President

Date: November 19, 1986

THE FIRST NATIONAL BANK OF
BOSTON
in its individual capacity
and as Owner Trustee

By: [Signature]
Assistant Vice President

Date: November 19, 1986

CHEMICAL BANK,
as Indenture Trustee

By: [Signature]
Vice President

Date: November 19, 1986

ARIZONA PUBLIC SERVICE
COMPANY

By: [Signature]
Vice President and Treasurer

Date: November 19, 1986

[II.7]

SECURED LEASE OBLIGATION BONDS, SERIES 1986
COMMITMENT AGREEMENT

November 19, 1986

PVNGS Funding Corp, Inc.
1209 Orange Street
Wilmington, Delaware 19801

\$273,000,000
Secured Lease Obligation Bonds, Series 1986

Gentlemen:


Reference is made to (i) the Underwriting Agreement dated November 6, 1986 (the Underwriting Agreement) among Arizona Public Service Company, an Arizona corporation (APS), PVNGS Funding Corp, Inc., a Delaware corporation (Funding Corp), and The First Boston Corporation, Kidder Peabody & Co. Incorporated and Salomon Brothers Inc, individually and as representatives of the other underwriters identified therein (collectively, the Underwriters), providing for the purchase by the Underwriters, severally, of \$273,000,000 aggregate principal amount of Funding Corp's Secured Lease Obligation Bonds, Series 1986 (the Bonds) and (ii) the Collateral Trust Indenture dated as of November 1, 1986 (the Indenture), as supplemented by the Series 1986 Bond Supplemental Indenture dated as of November 15, 1986 (the Series 1986 Bond Supplemental Indenture), each among APS, Funding Corp and Chemical Bank, as Trustee (the Trustee), pursuant to which the Bonds are to be issued.

1. If APS, in a timely manner, provides Funding Corp with information sufficient for Funding Corp to direct the adjustments described in Section 7.01 of the Indenture or Section 1.04(b) of the Series 1986 Bond Supplemental Indenture, as the case may be, Funding Corp shall deliver to the Trustee a Company Request pursuant to such Section 7.01 or Section 1.04(b).

2. This Commitment Agreement has been executed and delivered in the State of New York and shall be governed by, and be construed in accordance with, the laws of the State of New York.

ARIZONA PUBLIC SERVICE
COMPANY

By


Title: Vice President and Treasurer

Accepted and agreed:

PVNGS FUNDING CORP,
INC.

By


Vice President

TAX INDEMNIFICATION AGREEMENT

dated as of August 1, 1986

between

EMERSON FINANCE CO.
as Equity Participant

and

ARIZONA PUBLIC SERVICE COMPANY,
as Lessee

Sale and Leaseback of an Undivided Interest in
Palo Verde Nuclear Generating Station Unit 2

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TAX INDEMNIFICATION AGREEMENT

THIS TAX INDEMNIFICATION AGREEMENT, dated as of August 1, 1986, is between EMERSON FINANCE CO., a Delaware corporation (the "Equity Participant") and ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation (the "Lessee"). Capitalized terms not otherwise defined herein shall have the meaning set forth in Appendix A to the Participation Agreement, dated as of August 1, 1986, among Emerson Finance Co., Bank of America, National Trust and Savings Association, PVNGS Funding Corp., Inc., The First National Bank of Boston, Chemical Bank and Arizona Public Service Company (the "Participation Agreement").

W I T N E S S E T H:

To induce the Equity Participant to execute the Participation Agreement, to make its investment as contemplated therein, to cause the Owner Trustee to purchase the Undivided Interest and the Real Property Interest and thereby to become entitled to the income tax attributes associated with ownership of the Undivided Interest and each element and component thereof and the Real Property Interest, and to induce the Equity Participant to enter into the Trust Agreement and to cause the Owner Trustee to lease the Undivided Interest and the Real Property Interest to the Lessee, and in full consideration of the foregoing, the Lessee irrevocably agrees, upon and in conformity with the terms hereof, to pay to the Equity Participant the indemnities as hereinafter set forth:

SECTION 1. Tax Assumptions and Tax Representations.

(a) Tax Assumptions. The Facility Lease has been entered into, and the Equity Participant's Net Economic Return has been computed, on the basis, inter alia, of the following tax assumptions (it being understood that nothing in this Section 1(a) is intended as a representation or warranty of the Lessee, except as expressly set forth in Section 1(b)):

(1) The Facility Lease will be treated as a true lease; the Owner Trustee will be treated as the purchaser, owner and lessor of the Undivided Interest;

and the Lessee will be treated as the lessee of the Undivided Interest.

(2) The Trust will be treated as a grantor trust which is subject to Subpart E, Part I, Subchapter J, Chapter 1 of Subtitle A (sections 671 through 679 inclusive) of the Code and the Regulations thereunder; the Equity Participant will be treated as the owner of the entire Trust; and the Equity Participant will be entitled to take into account, in computing the consolidated federal income tax liability of the affiliated group of corporations of which the Equity Participant is a member (the "Group") each item of income, gain, loss, deduction and credit of the Trust.

(3) For purposes of claiming the investment tax credit, the Equity Participant and the Owner Trustee will elect to treat the Lessee as having acquired the Undivided Interest pursuant to section 48(d) of the Code.

(4) For purposes of computing cost recovery deductions under the Accelerated Cost Recovery System provided in section 168 of the Code ("ACRS") with respect to the Undivided Interest, the Owner Trustee's basis for federal income tax purposes (determined without regard to increases in basis attributable to expenditures made by or on behalf of the Owner Trustee or the Equity Participant and not included in the Purchase Price) (the "Owner Trustee's Basis") will be at least equal to the portion of the Purchase Price allocated to the Undivided Interest in Schedule 3 to the Participation Agreement.

(5) Cost recovery deductions under ACRS will be allowed with respect to the Undivided Interest pursuant to sections 167(a), 168(a) and 168(b)(1) of the Code; the Equity Participant's taxable year in which the Closing Date occurs will be a full taxable year; and, provided that no election is made by the Equity Participant under section 168(b)(3) of the Code, the Equity Participant will be entitled to take such deductions into account in computing the consolidated federal income tax liability of the Group, in the taxable year of the Equity Participant which includes the Closing Date and each of its nine succeeding taxable years, in an amount determined by applying the "Applicable Percentage" for each such taxable year to the Owner Trustee's Basis in the Undivided Interest in accordance with the following table:

<u>Taxable Year Ending</u> <u>September 30</u>	<u>Applicable Percentage</u>
1986	8%
1987	14%
1988	12%
1989	10%
1990	10%
1991	10%
1992	9%
1993	9%
1994	9%
1995	9%

(the deductions described in this paragraph (5) being hereinafter referred to as the "ACRS Deductions").

(6) The indebtedness evidenced by the Notes will constitute a loan made to the Owner Trustee; all amounts payable thereon as interest or premium will be deductible by the Equity Participant, when paid or accrued, pursuant to section 163 of the Code and the Regulations thereunder, in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income (the "Interest Deductions"); and the Equity Participant will be entitled to take the Interest Deductions into account in computing the consolidated federal income tax liability of the Group.

(7) The Equity Participant will be allowed current deductions for amortization of an amount equal to the Transaction Expenses computed on a straight-line basis over the Basic Lease Term (the "Amortization Deductions"); and the Equity Participant will be entitled to take the Amortization Deductions into account in computing the consolidated federal income tax liability of the Group.

(8) The Equity Participant will have at all relevant times sufficient federal taxable income against which to apply the ACRS Deductions, the Interest Deductions and the Amortization Deductions.

(9) The Notes will bear interest pursuant to their terms at the rates applicable from time to time; the principal amount of the Notes will constitute no more

than 80 percent of the Purchase Price; and the Notes will be amortized by certain payments of principal pursuant to the terms thereof.

(10) Basic Rent will be paid on December 30, 1986 and the Basic Rent Payment Dates. Basic Rent will be payable in semi-annual installments during the Basic Lease Term and each Renewal Term as set forth in the Facility Lease.

(11) Neither the Owner, Trustee nor the Equity Participant (i) will at any time prior to the end of the Lease Term be required to include any amount in gross income for federal income tax purposes in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such items of property, other than any such payments required to be made on an After-Tax Basis pursuant to the Transaction Documents and (ii) will at any time be required to include any other amount in gross income for federal income tax purposes with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than (a) payments of Basic Rent, in the amounts and no earlier than at the times such payments are accrued in accordance with the terms of the Facility Lease, which payments of Basic Rent shall be accrued ratably over the six-month period (or portion thereof in the case of Basic Rent payable on December 30, 1986) ending June 30, in the case of each payment of Basic Rent due June 30, and ending December 31, in the case of each payment of Basic Rent due December 30, (b) payments of Casualty Value, Special Casualty Value and Extraordinary Casualty Value at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income, (c) amounts paid to the Equity Participant which are specifically identified as interest, (d) any amount paid to the Equity Participant with respect to which the Equity Participant is entitled to a contemporaneous and fully offsetting deduction, (e) any payments required to be made on an After-Tax Basis pursuant to the Transaction Documents, at the time such payments are made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income, (f) payments pursuant to the exercise of Lessee's options to purchase the Undivided Interest as described in the

Facility Lease at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income and (g) payments pursuant to the sale or other disposition of the Undivided Interest, other than as described in clause (f), at the time such payments are required to be made and would be includable in accordance with the method of tax accounting on the basis of which the Equity Participant regularly computes its income.

(12) The Equity Participant's marginal federal rate of income tax is 46%, without giving effect to any credits against tax and such marginal rate will be applicable to each item of income and deduction contemplated by this Section 1(a).

(13) The Equity Participant's cash investment in the Undivided Interest will be an amount equal to no less than 20% of the Purchase Price.

(14) The Closing Date will be August 18, 1986.

(15) For federal income tax purposes, the taxable year of the Equity Participant is a fiscal year ending September 30, and the Equity Participant will report all items of income, gain, loss or deduction relating to the transactions contemplated by the Transaction Documents using the accrual method of tax accounting except as otherwise contemplated by Section 1(a)(11) hereof in respect of Basic Rent.

(16) The Owner Trustee and the Equity Participant will be entitled to treat each item of income, gain, loss, deduction and credit with respect to the transactions contemplated by the Transaction Documents and the Financing Documents as derived from or allocable to sources within the United States.

(17) The Equity Participant will not be subject to the imposition of any surtax, "clawback tax", "user fee" or similar imposition, or to any at-risk limitation or restriction on the utilization of passive losses by reason of its participation in the transactions contemplated by the Transaction Documents and the Financing Documents, nor otherwise suffer an adverse effect on its anticipated Net Economic Return by reason of a Change in Tax Law.

(b) Tax Representations. The Lessee represents and warrants to and covenants with the Equity Participant that:

(1) On the Closing Date and throughout the Lease Term, the Undivided Interest and each item of property constituting the Undivided Interest will be "recovery property" and "10-year property" within the meaning of sections 168(c)(1) and 168(c)(2)(C) of the Code as in effect on the Closing Date.

(2) Unit 2, the Lessee's undivided interest in Unit 2 and each item of property constituting the Undivided Interest will have been "placed in service" for federal income tax purposes on or before the Closing Date.

(3) No item of property constituting the Undivided Interest and no portion of the Purchase Price will be subject to the provisions of section 168(f)(12) of the Code. No item of property constituting the Undivided Interest and no portion of the Purchase Price will be subject to the provisions of section 168(f)(10) of the Code.

(4) The Lessee has provided to the Ebasco Business Consulting Company all factual information in its possession which is relevant to the conclusions of Ebasco Business Consulting Company and such information is accurate and complete on the Closing Date. The Lessee has no reason to believe that the conclusions of Ebasco Business Consulting Company are inaccurate.

(5) Assuming that the Owner Trustee is the owner of the Undivided Interest for federal income tax purposes, the Equity Participant will be entitled to the ACRS Deductions, the Interest Deductions and the Amortization Deductions.

(6) Neither the Owner Trustee nor the Equity Participant (i) will at any time prior to the end of the Lease Term be required to include any amount in gross income for Federal income tax purposes in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such items of property, other than any such payments required to be made on an After-Tax Basis pursuant to the Transaction Documents and (ii) will at any time be required to include any other amount in

gross income for federal income tax purposes with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts described in Sections 1(a)(11)(ii)(a) through (g) hereof at the respective times referred to therein.

(7) The Owner Trustee and the Equity Participant will be entitled to treat each item of income, gain, loss and deduction with respect to the transactions contemplated by the Transaction Documents or the Financing Documents as derived from or allocable to sources within the United States within the meaning of section 861 of the Code and the Regulations promulgated thereunder.

(8) At all times prior to the Closing, the Undivided Interest will have been owned by the Lessee.

(9) The Equity Participant will not lose any of the tax benefits expected to be available to it with respect to the transactions contemplated by the Transaction Documents by reason of the application of section 168(e) of the Code to the transactions contemplated by the Transaction Documents.

(10) Throughout the Lease Term the Undivided Interest will not constitute "tax-exempt use property" within the meaning of section 168(j) of the Code and the provisions of section 168(j) of the Code as in effect on the Closing Date will not apply to the transactions contemplated by the Transaction Documents.

(11) No part of the Undivided Interest will be used predominantly outside the United States within the meaning of section 168(f)(2) of the Code.

(12) On the Closing Date, no improvements, modifications or additions to Unit 2 or the Undivided Interest will be required to render Unit 2 or the Undivided Interest complete for its intended use by the Lessee.

(13) All of the cost of the Undivided Interest or the Real Property Interest paid for or incurred by the Lessee or any Affiliate thereof will in each case have been reimbursed by the Owner Trustee through payment of the Purchase Price and the Real Estate Investment, respectively.

(14) On the Closing Date, the fair market value of the Undivided Interest will be the amount set forth as the Purchase Price in Schedule 3 to the Participation Agreement and the fair market value of the Real Property Interest will be the amount set forth as the Real Estate Investment in Schedule 3 to the Participation Agreement; and, assuming that the Owner Trustee is the owner of the Undivided Interest for federal income tax purposes, the Owner Trustee's Basis in the Undivided Interest and the Real Property Interest will in each case be at least equal to the Purchase Price and the Real Estate Investment, respectively.

(15) (i) It is reasonable to expect (x) that the Undivided Interest will be useful to and useable by a Person other than the Lessee or any Person related (within the meaning of section 318 of the Code) to the Lessee at the end of the Basic Lease Term and any Fixed Rate Renewal Term and capable of lease or transfer to such a Person at that time, and (y) that it will be commercially feasible for the Owner Trustee or the Equity Participant to enter into such a lease or transfer at such time in a transaction pursuant to which the Equity Participant would realize, with respect to the Undivided Interest, the residual value set forth in the report of Ebasco Business Consulting Company apart from any amounts that such a Person would be required to expend pursuant to the Assignment and Assumption or otherwise in connection with the acquisition or use of the Undivided Interest and apart from any amounts that such a Person would be required to expend in connection with the acquisition or use of the Real Property Interest and (ii) the Undivided Interest does not constitute, and will not constitute during the Lease Term, "limited use property" within the meaning of Revenue Procedure 76-30; provided, however, that this representation is not a representation that any residual value will in fact exist at the end of the Basic Lease Term and any Renewal Term.

(16) With respect to the Undivided Interest and the indebtedness evidenced by the Notes, neither the Lessee, any Affiliate nor any Person claiming by, through or under the Lessee or any Affiliate (other than the Owner Trustee, Equity Participant or any successor thereto) will at any time claim the ACRS Deductions, the Interest Deductions, the Amortization Deductions or any corresponding deduction under applicable state or local income tax law.

(17) The Equity Participant will not be required pursuant to section 467 of the Code to include in gross income any Rent at any time earlier than the time such payments are accrued in accordance with the terms of the Facility Lease.

(18) The Lessee does not legally or beneficially or constructively own (within the meaning of section 318 of the Code) any capital stock of the Loan Participants, Original Loan Participants, Funding Corp or any Holder of Bonds.

(19) Neither the Equity Participant nor the Owner Trustee will be treated as engaged in a partnership with any other Person as a result of the transactions contemplated by the Transaction Documents or the Financing Documents.

SECTION 2. Indemnification.

(a) Consistent Tax Returns. The Lessee agrees that neither it nor any Affiliate will at any time take any action, directly or indirectly, or file any returns or other documents inconsistent with the assumptions and representations set forth in Section 1 hereof, and that the Lessee and any such Affiliate will file such returns, maintain such records, take such actions and execute such documents, as reasonably requested by the Equity Participant from time to time, and as may be appropriate to facilitate the realization of such assumptions by the Equity Participant. The Lessee covenants and agrees to maintain, or cause to be maintained, such other records as shall be reasonably requested by the Equity Participant, in each case in order to verify the factual basis for the matters referred to in this Tax Indemnification Agreement. The Lessee shall make the records referred to in the preceding sentences (other than the Lessee's tax returns) available, or cause such records to be made available, for inspection by the Equity Participant or its authorized agents, during normal business hours at the Lessee's office at 411 North Central Avenue, Phoenix, Arizona 85072, Attention: Paul A. Williams, Vice President & Treasurer, upon request by, and five days' prior notice from, the Equity Participant. The Lessee shall, at its expense, upon request by the Equity Participant, provide to the Equity Participant a copy of such records which shall be certified to be a true copy by an affidavit attached thereto and executed by an officer of the Lessee. Notwithstanding the preceding sentence, the Equity

Participant or its authorized agents shall have the right to make copies and extracts of any such records at the Equity Participant's sole expense. The Lessee may, in accordance with its record retention practice and consistent with the requirements of the NRC, after written notice to the Equity Participant at least 30 days prior thereto, destroy such records as are specified in such notice other than those identified by the Equity Participant by written notice to the Lessee prior to such destruction.

(b) Indemnification--Loss of Tax Benefits. The Lessee shall indemnify the Equity Participant on an After-Tax Basis for,

(1) any loss, disallowance, delay in obtaining, or recapture of the ACRS Deductions, the Interest Deductions or the Amortization Deductions; any loss, disallowance, delay in obtaining, or recapture of any credits for foreign taxes that otherwise would have been allowable to the Equity Participant; or any inclusion in gross income of any amount with respect to the transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts set forth in Section 1(a)(11) hereof, at any time other than the times specified in Section 1(a)(11) hereof, in each case resulting in whole or in meaningful part from any one or more of the following events or circumstances:

(i) any representation or warranty of the Lessee in Section 1(b) hereof or elsewhere in this Tax Indemnification Agreement, the other Transaction Documents, the Financing Documents or any certificate or other document delivered by the Lessee in connection herewith or therewith, proving inaccurate at any time or the Lessee breaching any of its covenants in Section 1(b) hereof or any of its agreements, covenants, duties, undertakings or other obligations under this Tax Indemnification Agreement or the other Transaction Documents or the Financing Documents, or

(ii) any act or failure to act by the Lessee or by any Affiliate, transferee, sublessee, or assignee of the Lessee or by any user of the Undivided Interest, or by any person to whom the Lessee or any Affiliate thereof shall sell power or energy generated at PVNGS, or by any person having custody or possession of Unit 2 or the Undivided Interest or by any ANPP Participant or by any Affiliate of any

of the foregoing or by any subsequent transferee, sublessee or assignee or by any trustee, receiver, liquidator or debtor in possession of any of the foregoing, other than, in the case of the Lessee, the execution and delivery of one or more of the Transaction Documents or the Financing Documents and acts specifically required or expressly permitted to be performed by the Lessee under the Facility Lease or any Transaction Document or any Financing Document; provided, however, that (A) any act of the Lessee performed to satisfy a general covenant to comply with Applicable Laws or prudent utility practice or to cause the Undivided Interest to be operated and maintained or to carry out obligations under the ANPP Participation Agreement and related agreements, (B) any act that is permitted by implication or because it is not required or prohibited by such documents, (C) any act that implements a general requirement or right on the part of the Lessee in a manner that is not specifically required or expressly permitted under such documents, (D) the transfer, assignment, sublease or any other disposition (whether by merger or otherwise) by the Lessee, or any use by a Person other than the Lessee, of all or any part of its interest in the Undivided Interest and (E) the making of any Capital Improvement shall each be an act or failure to act for which the lessee is responsible under this paragraph (ii), or

(iii) the sale or other disposition of Unit 2, the Undivided Interest or any item of property constituting the Undivided Interest upon the exercise by the Equity Participant of its remedies under the Facility Lease upon the occurrence of an Event of Default thereunder, or

(iv) the bankruptcy, or other proceedings for the protection of debtors, of or involving the Lessee or any transferee, sublessee or assignee of the Lessee or any subsequent transferee, sublessee or assignee or any Affiliate of any of the foregoing, or any foreclosure on any property of any of the foregoing, or

(v) any damage to or destruction, loss of generating capacity, theft, nongovernmental taking or requisition or repair of or any addition, improvement, modification, alteration, replacement

or substitution of or to Unit 2 or the Undivided Interest or the Real Property Interest, or any part thereof, or any Event of Loss or Deemed Loss Event, or any event which, with the passage of time or the giving of notice or both, would constitute such an event, or

(vi) any governmental taking or requisition of title, use or otherwise of Unit 2, the Undivided Interest or the Real Property Interest or any part thereof if such taking or requisition does not immediately constitute an Event of Loss under the Facility Lease, or

(vii) any payment by any manufacturer or any other vendor or supplier or contractor or subcontractor with respect to any part of Unit 2 or the Undivided Interest, but in the event of any such payment made to the Equity Participant, any indemnity hereunder shall take into account any economic benefit realized by the Equity Participant from the receipt of such payment without double counting for any economic loss for which such payment provided compensation, or

(viii) any issuance, defeasance, refinancing, refunding, redemption, purchase, repurchase, cancellation, retirement, reamortization, reoptimization, substitution, releveraging, modification or remarketing of the Notes, or the Bonds, or any other debt securities issued or assumed pursuant to the Transaction Documents or the Financing Documents or any terms or provisions thereof or otherwise in connection with the financing, refinancing or any Supplemental Financing of Unit 2, any Capital Improvement or the Undivided Interest or the Real Property Interest or any part thereof or interest therein, including, without limitation, the purchase or deemed purchase by the Lessee, Funding Corp, the Loan Participants or the Original Loan Participants of any such Notes, Bonds or securities, or the existence of any of the Lessee's rights to effect any of the foregoing, or

(ix) the presence of Funding Corp, or any successor or assign thereof, in the transactions contemplated by the Transaction Documents and the Financing Documents, or

(x) the existence or operation of the ANPP Participation Agreement, the ANPP Project Agreements or any amendment to any of the foregoing (including without limitation the rights and remedies of the ANPP Participants) or any obligations of the Lessee or restriction of rights of the Owner Trustee or the Equity Participant or provisions of any of the Transaction Documents or the Financing Documents (including without limitation the provisions of the Assignment and Assumption) resulting from any of the foregoing, or

(xi) the existence, provisions or operation of the License or the License Amendment, or

(xii) the existence, provisions or operation of Title USA Company of Arizona Trust No. 530, or

(xiii) the existence or implementation of the provisions (w) set forth in Section 10(b)(3)(ix) of the Participation Agreement relating to the rights of the Lessee to purchase the Undivided Interest if it fails to renew the Letter of Credit, (x) set forth in Section 10(b)(3)(viii) of the Participation Agreement, (y) set forth in Section 5 of the Facility Lease and Sections 15(iii) and 16(a)(vii) of the Facility Lease and (z) providing for Deemed Loss Events, or

(xiv) without limiting the generality of the foregoing clause (xiii) of this Section 2(b)(1), the maintenance or creation of any decommissioning fund pursuant to Section 10(b)(3)(viii) of the Participation Agreement (the "Decommissioning Fund"); the investment or the failure to invest money held in the Decommissioning Fund; the earning of investment income, the failure to earn investment income or the realization of any gain or loss with respect to the investment of money held in the Decommissioning Fund; or any act or failure to act with respect to the Decommissioning Fund (whether or not such act or failure to act is permitted or required under the Transaction Documents or the Financing Documents) of the trustee of either thereof, the Lessee, any Affiliate of the Lessee or any other Person,

(2) any inclusion in the Equity Participant's gross income, for federal income tax purposes, of any amount in respect of any replacement or substitution of, or any alteration to or modification in any item of property constituting the Undivided Interest or any part thereof or any expenditures made or property furnished by the Lessee in respect of such item of property or pursuant to the Transaction Documents or Financing Documents (whether or not permitted or required under the Transaction Documents or Financing Documents) or any inclusion prior to the end of the Lease Term in the Equity Participant's gross income, for federal income tax purposes, of any amount in respect of any addition or improvement to any item of property constituting the Undivided Interest or any part thereof or the Real Property Interest or any expenditure made or property furnished by the Lessee in respect of such item of property or pursuant to the Transaction Documents or Financing Documents (whether or not permitted or required under the Transaction Documents or Financing Documents) and

(3) any loss, disallowance, delay in obtaining or recapture of the ACRS Deductions, the Interest Deductions or the Amortization Deductions; any loss, disallowance, delay in obtaining or recapture of any credits for foreign taxes that otherwise would have been allowed to the Equity Participant; any inclusion in gross income of any amount with respect to any transactions contemplated by the Transaction Documents or the Financing Documents other than the amounts set forth in Section 1(a)(11) hereof, at any time other than the times specified in Section 1(a)(11) hereof; or the imposition of any restriction on the use of any benefit contemplated by the assumptions set forth in Section 1(a) hereof or the imposition of any surtax or similar imposition or suffering described in Section 1(a)(17) hereof, in each case resulting in whole or in part from a Change in Tax Law

(any such loss, disallowance, delay in obtaining, recapture, imposition or inclusion in respect of either subsection (1) or (2) above or this subsection (3) being hereinafter referred to as a "Tax Loss").

(c) Indemnity Payment - After-Tax Basis.

(1) In the event of a Tax Loss, the Equity Participant, unless pursuant to Section 5 hereof the Equity Participant is not entitled to payment with respect to such

Tax Loss, shall give notice in writing to the Lessee of such Tax Loss accompanied by a written statement describing in reasonable detail such Tax Loss and the computation of the amount payable, and the Lessee shall pay to the Equity Participant on an After-Tax Basis in a lump sum on the Effective Date an amount (the "Indemnity Payment") which, after giving effect to such Tax Loss and any interest, penalties or additions to tax payable as a result of such Tax Loss, will be sufficient to provide the Equity Participant the same Net Economic Return (after taking into account any future loss or losses of federal income tax benefits, and any past, present or future federal income tax benefits expected to be available to the Equity Participant, in each case, in the reasonable determination of the Equity Participant, generated as a result of the Tax Loss with respect to which the Indemnity Payment is being determined, the circumstances giving rise thereto or the determination thereof) that the Equity Participant would have realized if it had not suffered such Tax Loss.

(2) Notwithstanding the foregoing, if (a) the Lessee shall have provided a letter of credit or other financial support to the Equity Participant in amount, form and substance satisfactory to the Equity Participant in its sole discretion and (b) no Event of Default shall have occurred and be continuing, the Lessee may elect to pay an Indemnity Payment in equal semiannual payments to the Equity Participant (which payments do not constitute Basic Rent) on each Basic Rent Payment Date during the Basic Lease Term, commencing with the Effective Date; provided, however, that the amount of such payments shall in all events be calculated in a manner which preserves the Equity Participant's Net Economic Return. The Lessee shall give notice in writing to the Equity Participant of its election as to the mode of payment of any Indemnity Payment no later than 10 Business Days prior to the Effective Date of such Indemnity Payment.

SECTION 3. Determination of Payments.

Whenever it may be necessary for purposes of this Tax Indemnification Agreement to determine (a) the amount of any Tax Loss suffered by the Equity Participant or (b) the amount of any past, present or future tax benefits reasonably expected to be available to it, such determination shall be made on the assumptions that (a) the income taxes of the Equity Participant are payable at the marginal federal tax rate set forth in Section 1(a)(12) hereof, as such assumed marginal rate may

be modified to reflect a different marginal federal tax rate as a result of an adjustment to Basic Rent pursuant to Section 3(d) of the Facility Lease in connection with a Change in Tax Law (the "Effective Rate"), (b) in computing its federal income tax liability, the Equity Participant could have fully utilized the tax benefits that are the subject of such Tax Loss against taxes payable at the Effective Rate and (c) the Equity Participant can fully utilize any tax benefits required to be taken into account under Section 2(c)(1) hereof resulting from a Tax Loss against federal income taxes payable at the Effective Rate.

The determination of the amount payable to or by the Equity Participant under this Tax Indemnification Agreement shall be made in the first instance by the Equity Participant, who shall furnish the Lessee with a notice setting forth in reasonable detail the computations and methods used in computing such amount; and, if requested by the Lessee, such determination shall be verified in writing by a firm of nationally recognized independent public accountants selected by the Equity Participant and acceptable to the Lessee, provided that, if a firm of nationally recognized independent public accountants regularly audits the books of the Equity Participant, then such firm shall be deemed to be acceptable to the Lessee. The costs of such verification shall be borne by the Lessee unless, as a result thereof, the amount payable to the Equity Participant is less than the amount originally determined by the Equity Participant by 10 percent or more of such amount in which case such costs shall be paid by the Equity Participant. Any statements furnished to the Lessee pursuant to Section 3 hereof shall (a) be signed by a Responsible Officer of the Equity Participant, (b) state in reasonable detail the basis upon which such amount or adjustment has been determined and (c) certify that such amount or adjustment has been determined pursuant to and in compliance with this Tax Indemnification Agreement. The Lessee agrees that it will not have the right to inspect the tax returns, books, records or any other documents of the Equity Participant or any Affiliate thereof in order to verify the basis or the accuracy of the calculations so made or of the amounts set forth in any such statement and that the determinations made by the independent accountants in accordance with this Section 3 shall be conclusive and binding.

SECTION 4. Effective Date.

An Indemnity Payment shall be due and payable 20 days after the date of the Equity Participant's notice to the

Lessee pursuant to Section 2(c)(1) hereof, or in the case of an Indemnity Payment relating to a Tax Loss which results from a proposed adjustment of the IRS that was contested pursuant to Section 6 hereof, 20 days after a Final Determination (as defined in Section 6(e) hereof) with respect to such Tax Loss; provided, however, that if the Lessee elects to pay an Indemnity Payment by way of semiannual payments pursuant to Section 2(c)(2) hereof, such payments shall commence on the first Basic Rent Payment Date occurring after the date of the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or, in the case of an Indemnity Payment relating to a Tax Loss that results from a proposed adjustment of the IRS that is contested pursuant to Section 6 hereof, on the first Basic Rent Payment Date occurring 20 days or more after a Final Determination with respect to such Tax Loss (the "Effective Date"). Notwithstanding anything to the contrary contained in the foregoing portion of this Section 4, and subject to Section 6 hereof as described below in this sentence, in the event of the expiration of the Basic Lease Term or the earlier termination of the Lease prior to the Effective Date of any Indemnity Payment, the Lessee shall pay to the Equity Participant on demand in a lump sum any such Indemnity Payment to the extent then unpaid; provided, however, that in no event shall the Lessee be required to pay all or any portion of any such Indemnity Payment prior to (x) the date 20 days after the date of the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or (y) if any such Indemnity Payment relates to a Tax Loss that is contested pursuant to Section 6 hereof, the date 20 days after the date of a Final Determination with respect to such Tax Loss. If pursuant to Section 3 hereof the Lessee requests verification of the computation of an Indemnity Payment, and such verification is not complete on the Effective Date then (i) the Lessee shall pay to the Equity Participant on the Effective Date the amount of the Indemnity Payment set forth in the Equity Participant's notice to the Lessee pursuant to Section 2(c)(1) hereof or the amount of the semiannual payment pursuant to Section 2(c)(2) hereof then due and payable, as the case may be, (ii) if the verification results in an upward adjustment to such Indemnity Payment or semiannual payment, the Lessee shall pay to the Equity Participant within 5 days after such verification is complete the amount of such upward adjustment with interest at the Prime Rate from the Effective Date to the date of payment and (iii) if the verification results in a downward adjustment to such Indemnity Payment or semiannual payment, the Equity Participant shall reimburse to the Lessee within 5 days after such verification is complete the amount

of such downward adjustment with interest at the Prime Rate from the Effective Date to the date of payment.

SECTION 5. Excluded Events.

The Equity Participant shall be responsible for, and shall not be entitled to any payment in respect of any Tax Loss occurring primarily as a direct result of one or more of the following events:

(a) a failure of the Equity Participant to claim in a proper or timely manner the ACRS Deductions, the Interest Deductions or the Amortization Deductions for the appropriate years (any disclosure or failure to make a disclosure pursuant to section 6661 of the Code shall not cause a claim to be considered improper), unless (i) the claiming of any such deductions would be inconsistent with any prior audit adjustment by the IRS with respect to which the Lessee is required to indemnify the Equity Participant under this Tax Indemnification Agreement (except to the extent such prior audit adjustment is being contested in accordance with the provisions of Section 6 hereof), (ii) the Equity Participant shall have furnished the Lessee, at the Lessee's sole cost and expense, with an opinion of independent tax counsel (selected by the Equity Participant and reasonably satisfactory to the Lessee) to the effect that as a result of a Change in Tax Law, Event of Loss, Deemed Loss Event, Termination Event, or an act, omission or misrepresentation of the Lessee such claim would not be proper pursuant to the standards of ABA Formal Opinion 85-352 or (iii) such failure to claim any such deductions for the appropriate year is caused by a failure of the Lessee to take any action or provide the Equity Participant with any information or document that the Lessee is required to take or provide pursuant to the Transaction Documents or the Financing Documents;

(b) the failure of the Equity Participant to have sufficient federal taxable income to benefit from the ACRS Deductions, the Interest Deductions, or the Amortization Deductions; provided, however, that such failure shall not be taken into account in determining the amount of any indemnity otherwise payable hereunder;

(c) any voluntary sale by the Equity Participant or any involuntary sale or other disposition resulting from the bankruptcy of, the foreclosure against, or any

similar proceeding against, the Equity Participant or the Owner Trustee, of the Undivided Interest, the Trust Estate, or any beneficial interest therein, unless such bankruptcy, foreclosure or similar proceeding relates to the transactions contemplated by the Transaction Documents, or an Event of Default shall have occurred and be continuing;

(d) (i) any Event of Loss or Deemed Loss Event whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, Casualty Value or Special Casualty Value for all of the Undivided Interest, (ii) any termination of the Facility Lease, whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, Casualty Value or Extraordinary Casualty Value for all of the Undivided Interest, or (iii) the exercise of the Cure Option, whereby the Lessee is required under the Facility Lease to pay, and shall have paid in full, the greater of Fair Market Sales Value and Casualty Value for all of the Undivided Interest except to the extent the payment made with respect to such Event of Loss, Deemed Loss Event, termination or exercise did not properly reflect the time of the occurrence of such Event of Loss, Deemed Loss Event, termination or exercise;

(e) any amendment, modification, deletion, addition or change in or to the provisions of the Code which shall occur after the Closing Date; provided, however, that the foregoing exclusion shall not apply (i) to a Change in Tax Law unless there has been a rent adjustment pursuant to Section 3(d) of the Facility Lease for such Change in Tax Law and (ii) to any Tax Loss which results from the inaccuracy of any representation made after the Closing Date by the Lessee in connection with a Change in Tax Law, and provided, further, that the foregoing exclusion shall not apply if such Tax Loss is a result in whole or in meaningful part of any act or failure to act (other than any act specifically required or expressly permitted to be performed by the Lessee under the Facility Lease or any Transaction Document, subject to the proviso in Section 2(b)(1)(ii) hereof), after the date of enactment of such amendment, modification, deletion, addition or change, by any person referred to in Section 2(b)(1)(ii) hereof;

(f) the application of Section 168(f)(5) of the Code to the Equity Participant solely because any taxable year of the Equity Participant is not a full taxable year;

(g) the inability of the Equity Participant to claim the ACRS Deductions, the Interest Deductions or the Amortization Deductions due to the Equity Participant or any Affiliate thereof or any predecessor of any thereof, being or becoming an entity subject to the provisions set forth in section 168(e)(3), 168(f)(11), 168(j), 465, 501, 593, 851, 856, 871, 881, 1361, 1381, 1391 or other similar provision of the Code relating to the status of the Equity Participant, unless such inability results from (i) in the case of section 168(e)(3) of the Code, the transactions contemplated by the Transaction Documents or (ii) a Change in Tax Law;

(h) the failure of the transaction to qualify as a "true lease" for federal income tax purposes, resulting in the Equity Participant not being treated as the owner of the Undivided Interest for federal income tax purposes, unless such failure is the result in whole or in meaningful part of an event or circumstance set forth in Section 2(b) hereof;

(i) the failure of the Equity Participant to fulfill its material obligations to contest a proposed adjustment or adverse determination as provided in Section 6 hereof; and

(j) the failure of the Owner Trust to be taxed as a conduit entity unless such failure arises as the result of an event or circumstance set forth in Section 2(b).

SECTION 6. Contests.

For purposes of defining the amount, if any, of Lessee's indemnity obligations hereunder:

(a) If the IRS proposes in writing an adjustment to the federal income tax liability of the Equity Participant, which adjustment, if sustained, would result in a Tax Loss, the Equity Participant shall notify the Lessee promptly of such adjustment and of all action taken or proposed to be taken by the IRS, and the Equity Participant shall for at least 30 days after giving such notice forbear, if such forbearance is permitted by law, payment of any tax (including interest, penalties and additions to tax thereon) asserted to be payable as a result of such proposed adjustment.

(b) If the Lessee requests within 30 days after the Equity Participant's notice pursuant to paragraph (a) of this Section 6 that the proposed adjustment be contested, the Equity Participant shall contest the proposed adjustment in good faith at the trial court level upon receipt of an opinion, furnished at the Lessee's sole cost and expense and setting forth the facts and legal analysis on which it is based, of independent tax counsel of nationally recognized standing selected by the Equity Participant and reasonably satisfactory to the Lessee to the effect that there exists a basis in law and fact under the standard imposed by ABA Formal Opinion 85-352 for such contest and at each appellate level upon receipt of an opinion furnished at the Lessee's sole cost and expense and setting forth the facts and legal analysis on which it is based, of independent tax counsel of nationally recognized standing selected by the Equity Participant and reasonably satisfactory to the Lessee to the effect that it is more likely than not that an appellate court will reverse or substantially modify the lower court decision, provided that (i) the Equity Participant shall be entitled to pursue or forego any administrative proceedings (except that the Equity Participant shall be required to pursue all reasonable administrative proceedings in the event judicial proceedings shall be unavailable by reason of a Tax Loss decreasing a net operating loss carryover, and in all events, the Equity Participant shall be required to pursue such administrative proceedings as shall be necessary to preserve available judicial proceedings), shall be required to contest any proposed adjustment beyond the level of administrative proceedings only if timely requested by the Lessee and shall not be required to pursue any appeal to the United States Supreme Court, (ii) the Equity Participant shall determine the court of competent jurisdiction in which to contest the proposed adjustment either before or after payment of the tax asserted to be payable as a result thereof, and (iii) the Equity Participant shall keep the Lessee informed as to the progress of any litigation and, if requested by the Lessee, shall consult with the Lessee's counsel (provided that the conduct of all administrative proceedings and litigation shall nevertheless remain within the sole discretion of the Equity Participant and its tax counsel exercised in good faith and provided, further, that the Equity Participant shall not discriminate (except with respect to selecting the forum in which to contest such proposed adjustment) against any such proposed adjustment as compared to other proposed adjustments made by the IRS

involving the potential tax liability of the Equity Participant). The Equity Participant shall not be required to take any action pursuant to this paragraph (b) of this Section 6 unless: (i) the amount of the Indemnity Payment arising from all proposed adjustments with respect to a taxable year, plus all indemnities that would arise by reason of the fact that the subject matter of any such adjustments is of a continuing nature, shall be in excess of \$500,000; (ii) the Lessee shall have agreed to indemnify the Equity Participant in a manner satisfactory to the Equity Participant for any expense which the Equity Participant may incur as a result of contesting such proposed adjustment; (iii) the Lessee shall have agreed to pay the Equity Participant on demand all reasonable costs and expenses that the Owner Participant may incur in connection with contesting such proposed adjustment (including, without limitation, reasonable legal and accounting fees, disbursements, penalties, interest and additions to tax); (iv) the Lessee shall have acknowledged its liability to the Equity Participant for an Indemnity Payment pursuant to this Tax Indemnification Agreement as a result of such proposed adjustment if and to the extent the Equity Participant shall not prevail in the contest of such proposed adjustment; (v) no Event of Default shall have occurred and be continuing; and (vi) the Equity Participant shall have determined that the action to be taken will not result in any danger of sale, forfeiture or loss of, or the creation of any Lien (except for Liens permitted under the Transaction Documents and except if the Lessee shall have adequately bonded such Lien or otherwise made provision to protect the interests of the Equity Participant in a manner satisfactory to the Equity Participant) on the Undivided Interest, the Real Property Interest, Unit 2 or any part thereof or interest therein. The Equity Participant shall also not be required to contest any proposed adjustment if the subject matter thereof shall be of a continuing nature and shall have previously been decided pursuant to the contest provisions of this Section 6, unless, subject to the other provisions of this Section 6, there shall have been a change in the law (including, without limitation, amendments to statutes or regulations, administrative rulings and court decisions) after such previous contest shall have been so decided, and the Equity Participant shall have received an opinion, setting forth the facts and legal analysis on which it is based, of independent tax counsel selected as provided in this Section 6(b) and furnished at the Lessee's sole expense to the effect that

the prior authorities are no longer determinative of the issue and that under such new law there exists a basis in law and fact under the standard imposed by ABA Formal Opinion 85-352 to contest such proposed adjustment.

(c) If the Equity Participant shall elect to contest a proposed adjustment by paying the tax claimed (including such other amounts payable as interest, penalties, or additions to tax) and seeking a refund, and if the proposed adjustment would be a Tax Loss with respect to which the Lessee could be required to indemnify the Equity Participant under this Tax Indemnification Agreement, then the Lessee shall advance to the Equity Participant on an interest-free basis and with no additional net after-tax cost to the Equity Participant the aggregate amount of such taxes, interest, penalties and additions to tax which the Equity Participant shall have elected to pay. If the Equity Participant subsequently receives a refund (or if the Equity Participant would have received a refund but for the fact that funds advanced by the Lessee were applied in payment of a tax liability of the Equity Participant for which the Lessee is not required to make an Indemnity Payment pursuant to this Tax Indemnification Agreement) of such taxes, interest, penalties or additions to tax, the Equity Participant shall promptly pay to the Lessee the amount received (or which would have been received) as a refund of such taxes, interest, penalties or additions to tax plus the amount of any interest received (or which would have been received) by the Equity Participant from the taxing authority with respect to such refunded taxes, interest, penalties or additions to tax; provided, however, that the Equity Participant shall not be obligated to refund to the Lessee any amount applied to a tax liability of the Equity Participant (or interest with respect thereto) if the IRS would have been foreclosed from asserting such tax liability but for the contest of such proposed adjustment; and provided, further, that the Equity Participant may offset the amount of such refunded taxes, interest, penalties or additions to tax and interest received or avoided against any amount due and owing by the Lessee to the Owner Participant pursuant to this Tax Indemnification Agreement.

(d) Notwithstanding anything to the contrary contained in this Section 6, the Equity Participant may at any time decline to take any further action with respect to a proposed adjustment or may settle any

contest without the consent of the Lessee; provided, however, that if the Lessee has properly requested the Equity Participant to contest such proposed adjustment pursuant to paragraph (b) of this Section 6 and shall have duly complied with all of the terms of this Section 6, the Equity Participant shall thereby waive its right to any Indemnity Payment by the Lessee that would otherwise be payable by the Lessee pursuant to this Tax Indemnification Agreement in respect of such adjustment, including any indemnities arising solely from such adjustment in subsequent years or which would arise by reason of the fact that the subject matter of such adjustment is of a continuing nature, unless in either case the contest of the adjustment giving rise to such indemnities is not precluded by the Equity Participant so declining or settling. In such event, the Equity Participant shall, within 30 days of such notice, reimburse the Lessee for all amounts previously advanced by the Lessee to the Equity Participant pursuant to paragraph (c) of this Section 6 including any interest received by the Equity Participant or the payment of which is actually avoided by reason of payment of the tax claimed with funds advanced by the Lessee.

(e) If the Lessee shall have appropriately requested the Equity Participant to contest any proposed adjustment as above provided and shall have duly complied with all of the terms of this Section 6, the amount of the Lessee's liability for indemnification pursuant to this Tax Indemnification Agreement shall become fixed upon a Final Determination of the liability of the Equity Participant for the tax and any interest, penalties and additions to tax asserted to be payable as a result of such proposed adjustment. A "Final Determination" with respect to a Tax Loss shall mean (i) a decision, judgment, decree or other order by any court of competent jurisdiction, which decision, judgment, decree or other order has become final (i.e., when all allowable appeals have been exhausted by either party to the action to the extent required by this Section 6) or, in any case where judicial review shall at the time be unavailable by reason of the proposed adjustment involving a decrease in a net operating loss carryforward, a decision, judgment, decree or other order of an administrative official or agency of competent jurisdiction, which has become final (i.e., all administrative appeals have been exhausted by either party to the extent required by this Section 6), (ii) a closing agreement entered into under section 7121 of the Code or any other settlement agreement entered

into in connection with an administrative or judicial proceeding, or (iii) the expiration of the time for instituting a claim for refund, or if such a claim was filed, the expiration of the time for instituting suit with respect thereto. Notwithstanding anything in this Section 6 to the contrary, the Equity Participant shall not be required to make any payments to the Lessee under this Section 6 while there shall be an amount due and owing by the Lessee to the Equity Participant under any of the Transaction Documents, or if and for so long as an Event of Default shall have occurred and be continuing.

SECTION 7. Adjustments.

The tax assumptions and the Lessee's representations set forth in Sections 1(a) and 1(b) hereof shall be modified to the extent necessary and appropriate to reflect any adjustments to Basic Rent provided for in Section 3(d) or 3(e) of the Facility Lease or the payment of an Indemnity Payment so as to reflect any Change in Tax Law or any Tax Loss in the manner in which it was taken into account in computing such adjustment or Indemnity Payment.

SECTION 8. Affiliated Group.

For purposes of this Tax Indemnification Agreement, the term "Equity Participant" shall include any member of an affiliated group of corporations of which the Equity Participant is, or may become, a member if consolidated returns are or shall be filed for such affiliated group for federal income tax purposes.

SECTION 9. Duration.

The obligations and liabilities of the Equity Participant and the Lessee arising under this Tax Indemnification Agreement shall continue in full force and effect, notwithstanding the expiration or early termination of the Facility Lease, until all such obligations have been met and such liabilities have been paid in full, and shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

SECTION 10. Payments.

All payments to be made to the Equity Participant or the Lessee pursuant to this Tax Indemnification Agreement shall be made in immediately available funds to such bank \ and/or account in the continental United States for the account of the Equity Participant or the Lessee as from time to time the Equity Participant shall have directed the Lessee or the Lessee shall have directed the Equity Participant, as the case may be, in writing. If the date on which any payment to be made pursuant to this Tax Indemnification Agreement shall not be a Business Day, such payment shall be made on the next succeeding Business Day.

SECTION 11. Interest.

Interest at the Penalty Rate shall be payable on any amount not paid when due hereunder until such amount shall be paid.

SECTION 12. Notices.

All notices and other communications provided for herein shall be given to the Equity Participant or the Lessee, as the case may be, in the manner and to the appropriate address, and shall become effective, as provided in Section 17 of the Facility Lease.

SECTION 13. No Setoff.

Except in accordance with the express terms hereof, (a) no payment required to be made by the Lessee pursuant to this Tax Indemnification Agreement shall be subject to any right of setoff, counterclaim, defense, abatement, suspension, deferment or reduction, and (b) the Lessee shall have no right to terminate this Tax Indemnification Agreement, or to be released, relieved or discharged from any obligation or liability under this Tax Indemnification Agreement for any reason whatsoever except as expressly provided herein.

SECTION 14. Governing Law.

This Tax Indemnification Agreement shall be governed by and construed in accordance with the laws of the State of New York.

SECTION 15. Counterparts.

This Tax Indemnification Agreement may be executed in any number of counterparts, each of which so executed shall be deemed to be an original, and such counterparts together shall constitute and be one and the same instrument.

SECTION 16. Headings.

The headings of the sections of this Tax Indemnification Agreement have been inserted for convenience of reference only and shall in no way restrict or otherwise modify any of the terms or provisions hereof.

SECTION 17. Amendments, Supplements, etc.

Neither this Tax Indemnification Agreement nor any of the terms hereof may be amended, supplemented, waived or modified orally, but only by an instrument in writing signed by the party against which enforcement of such change is sought.

SECTION 18. No Duplication of Payment.

Nothing contained in the terms of this Tax Indemnification Agreement or any other Transaction Document shall be construed to require the Lessee to make any payment with respect to any Tax Loss more than once or to make any payments hereunder to the extent previously reflected in a rental adjustment pursuant to Section 3(d) of the Facility Lease, otherwise, the Lessee's obligations hereunder are absolute and unconditional and are payable independent of and from the Facility Lease, the Participation Agreement and any other circumstance whatsoever.

IN WITNESS WHEREOF, the Equity Participant and the Lessee have caused this Tax Indemnification Agreement to be duly executed by their respective officers thereunto duly authorized as of the date set forth below.

ARIZONA PUBLIC SERVICE COMPANY

By _____
Vice President

Dated: _____

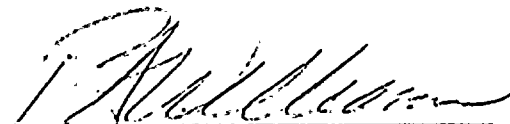
EMERSON FINANCE CO.

By W. L. Shays

Dated: 8-18-86

IN WITNESS WHEREOF, the Equity Participant and the Lessee have caused this Tax Indemnification Agreement to be duly executed by their respective officers thereunto duly authorized as of the date set forth below.

ARIZONA PUBLIC SERVICE COMPANY

By 
Vice President

Dated: 8-18-86

EMERSON FINANCE CO.

By _____

Dated:

REIMBURSEMENT AGREEMENT

between

Arizona Public Service Company

and

Morgan Guaranty Trust Company of New York

dated as of

August 1, 1986

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"Agreement" means this Reimbursement Agreement, as same may from time to time be amended, supplemented or modified.

"Business Day" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close.

"Code" means the United States Internal Revenue Code of 1954, as amended.

"Company Indenture" means the Mortgage and Deed of Trust dated as of July 1, 1946, as amended and supplemented at the date hereof, of Central Arizona Light and Power Company (now the Company) to Security-First National Bank of Los Angeles (now Security Pacific National Bank), as Trustee.

"Controlled Group" means all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Company, are treated as a single employer under Section 414(b) or 414(c) of the Code.

"Consolidated Subsidiary" means at any date any subsidiary or other entity the accounts of which would be consolidated with those of the Company in the Company's consolidated financial statements as of such date.

"Date of Early Termination" has the meaning set forth in the Letter of Credit.

"Date of Issuance" means the date on which the Letter of Credit is issued upon request of the Company pursuant to Section 3(a) hereof.

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

"Fixed Charge Ratio" has the meaning set forth in Section 7(i) hereof.

"Funded Indebtedness" means all Indebtedness which matures more than one year from the date of its creation or matures within one year from such date but is renewable or extendible, at the option of the Company, to a date more than one year from such date or arises under a revolving credit or similar agreement which obligates the lender or lenders to extend credit during a period of more than one year from such

date including, without limitation, all amounts of Funded Indebtedness required to be paid or prepaid within one year from the date of its creation.

"Guaranteed Indebtedness" of any Person means all Indebtedness referred to in clause (i), (ii) or (iii) of the definition of "Indebtedness" guaranteed directly or indirectly in any manner by such Person, or in effect guaranteed directly or indirectly by such Person through an agreement (i) to pay or purchase such Indebtedness or to advance or supply funds for the payment or purchase of such Indebtedness, or (ii) to purchase, sell or lease (as lessee or lessor) property, or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such Indebtedness or to assure the holder of such Indebtedness against loss, or (iii) to supply funds to or in any other manner invest in the debtor (including any agreement to pay for property or services irrespective of whether or not such property is received or such services are rendered), or (iv) otherwise to assure a creditor against loss.

"Imputed Rate" means, in respect of Indebtedness, the actual initial rate of interest to be paid by a Person with respect to such Indebtedness.

"Indebtedness" of any Person means (i) all indebtedness of such Person for borrowed money or for the deferred purchase price of property or services, (ii) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property acquired by such Person (even though the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property), (iii) all obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, recorded as capital leases in respect of which such Person is liable as lessee, (iv) all Operating Lease Obligations of such Person, (v) all Guaranteed Indebtedness, and (vi) all Indebtedness referred to in clause (i), (ii) or (iii) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any Lien upon or in property (including, without limitation, accounts and contract rights) owned by such Person, even though such Person has not assumed or become liable for the payment of such Indebtedness.

"Liens" means, with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind in respect of such asset. For the purposes of

this Agreement, the Company or any Subsidiary shall be deemed to own subject to a Lien any asset which it has acquired or holds subject to the interest of a vendor or lessor under any conditional sale agreement, capital lease or other title retention agreement relating to such asset.

"Material Subsidiary" means at any time a Subsidiary which as of such time meets the definition of a "significant subsidiary" contained as of the date hereof in Regulation S-X of the Securities and Exchange Commission.

"Maximum Credit Amount" means \$69,493,938.93.

"Maximum Drawing Amount" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"Operating Lease Obligations" of any Person means all obligations of such Person as lessee under each operating lease of all or a portion of any Unleased Interests.

"Outstanding Debt" of any Person means at any date, without duplication, (i) all obligations of such Person for borrowed money, (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business, (iv) all obligations of such Person as lessee under capital leases, (v) all Aggregate Operating Lease Obligations of such Person, (vi) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, (vii) all Outstanding Debt of others secured by a Lien on any asset of such Person, whether or not such Outstanding Debt is assumed by such Person, and (viii) all obligations, contingent or otherwise, of such Person directly or indirectly guaranteeing any Outstanding Debt of any other Person or in any manner providing for the payment of any Outstanding Debt of any other Person or otherwise protecting the holder of such Outstanding Debt against loss (whether by agreement to keep-well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), excluding, however, from this clause (viii) endorsements for collection or deposit in the ordinary course of business.

"Participant" has the meaning set forth in Section 14 hereof.

"PBGC" means the Pension Benefit Guaranty Corporation and any entity succeeding to any or all of its functions under ERISA.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" means at any time an employee pension benefit plan which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Code and is either (i) maintained by a member of the Controlled Group for employees of a member of the Controlled Group or (ii) maintained pursuant to a collective bargaining agreement or any other arrangement under which more than one employer makes contributions and to which a member of the Controlled Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions.

"Reimbursement Default" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"Reimbursement Event of Default" has the meaning set forth in Section 9 hereof.

"Subsidiary" means any corporation or other entity of which securities or other ownership interests having ordinary voting power to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by the Company or one or more Subsidiaries, or by the Company and one or more Subsidiaries.

"Successor Participant" means each Person to whom a Participant transfers all or a part of its participation with the consent of the Company.

"Tax" and "Taxes" have the meanings set forth in Section 2(c)(iii) hereof.

"Termination Date" means the earlier of (i) the date on which the Bank pays a drawing under the Letter of Credit for the Maximum Drawing Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of

ly Termination, (iii) if a drawing is requested by the
ity Participant after a notice of termination is given
under the Letter of Credit, the date on which the Bank pays
such drawing, (iv) the date on which the Company pays the
amounts due under Section 9(c) of the Facility Lease, (v) the
date on which the Company pays the amounts due under Section
9(d) of the Facility Lease [defaults] or (vi) either (x) the
fifth anniversary of the Date of Issuance of the Letter of
Credit or (y) if a draft and certificate all in strict con-
formity with the terms and conditions of the Letter of Credit
are presented after 10:00 a.m. but prior to 5:00 p.m. (New
York time) on the fifth anniversary of the Date of Issuance of
the Letter of Credit, the Business Day following such fifth
anniversary.

"Unfunded Vested Liabilities" means, with respect to
any Plan at any time, the amount (if any) by which (i) the
present value of all vested nonforfeitable benefits under such
Plan exceeds (ii) the fair market value of all Plan assets
allocable to such benefits, all determined as of the then most
recent valuation date for such Plan, but only to the extent
that such excess represents a potential liability of a member
of the Controlled Group to the PBGC or the Plan under Title IV
of ERISA.

"Unit 3" means the 1270 megawatt unit, commonly
known as Unit 3, at the Palo Verde Nuclear Generating Station,
together with all capital improvements thereto.

"Unleased Interests" means any real or personal or
mixed property interest of any Person in that portion of
Unit 2 and Unit 3 of the Palo Verde Nuclear Generating Station
which is not subject to an operating lease immediately after
the Letter of Credit has been issued by the Bank.

(b) Accounting Terms and Determinations. Unless
otherwise specified herein, all accounting terms used herein
shall be interpreted, all accounting determinations hereunder
shall be made, and all financial statements required to be
delivered hereunder shall be prepared in accordance with
generally accepted accounting principles as in effect from
time to time, applied on a basis consistent (except for chan-
ges concurred in by the Company's independent public account-
ants) with the most recent audited consolidated financial
statements of the Company and its Consolidated Subsidiaries
delivered to the Bank.

SECTION 2. Reimbursement. (a) The Company agrees
to pay to the Bank (i) not later than 2:00 p.m. New York City

time on the same Business Day on which the Bank shall pay any draft under the Letter of Credit a sum equal to the amount so paid under the Letter of Credit and (ii) interest on any and all amounts unpaid by the Company when due under clause (i) above from and including the date such amount is paid by the Bank under the Letter of Credit until payment in full, payable on demand, at a fluctuating interest rate per annum equal to 2% per annum above the rate of interest publicly announced by the Bank in New York City from time to time as its prime rate, but such fluctuating interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law.

(b) The Company agrees to pay to the Bank (i) a fee with respect to the Letter of Credit equal to .56834% per annum of the Maximum Credit Amount from the Date of Issuance to, but excluding, the Termination Date and (ii) an additional fee computed in accordance with the terms of the letter from the Bank to the Company dated August 1, 1986, in each case payable quarterly in arrears on each February 15, May 15, August 15 and November 15, and on the Termination Date, commencing November 15, 1986, provided that if Moody's Investors Service Inc. ("Moody's") shall rate the debt issued under the Company Indenture lower than Baa3 (or an equivalent rating if the rating system used by Moody's is revised) or Standard & Poor's Corporation ("S&P") shall rate such debt lower than BBB- (or an equivalent rating if the rating system used by S&P is revised), the fee payable pursuant to clause (i) above shall be increased by .15% per annum during the period commencing on the day on which either rating is so lowered to, but excluding, the first day thereafter on which both ratings are at least Baa3 and BBB-, respectively. The Company further agrees to pay to the Bank on the Date of Issuance an initial fee equal to .195% of the Maximum Credit Amount.

(c) (i) If after the date hereof, the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal

Reserve System) against letters of credit issued by or assets, deposits with or for the account of the Bank or shall impose on the Bank any other condition regarding this Agreement or the Letter of Credit and the result of the foregoing shall be to increase the cost to the Bank of issuing or maintaining the Letter of Credit (which increase in cost shall be the result of the Bank's reasonable allocation of the aggregate of such cost increases resulting from such events), then, within 15 days after demand by the Bank, the Company shall pay to the Bank all additional amounts which are necessary to compensate the Bank for such increased cost incurred by the Bank.

(ii) If after the date hereof, the Bank shall have determined that the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by the Bank with any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency, has or would have the effect of reducing the rate of return on the Bank's capital as a consequence of its obligations hereunder to a level below that which the Bank could have achieved but for such adoption, change or compliance (taking into consideration the Bank's policies with respect to capital adequacy) by an amount deemed by the Bank to be material, then within 15 days after demand by the Bank, the Company shall pay to the Bank such additional amount or amounts as will compensate the Bank for such reduction.

(iii) All payments made by the Company under this Agreement shall be made free and clear of, and without reduction for or on account of, any stamp or other taxes, levies, imposts, duties, charges, fees, deductions, withholdings, restrictions or conditions of any nature whatsoever hereafter imposed, levied, collected, withheld or assessed by any country (or by any political subdivision or taxing authority thereof or therein), except for franchise taxes and changes in the rate of tax on the overall net income of the Bank (such nonexcluded taxes being called "Tax" or "Taxes"). If any Taxes are required to be withheld from any amounts payable to the Bank, the amounts so payable to the Bank shall be increased to the extent necessary to yield to the Bank (after payment of all Taxes) interest or any such other amounts payable hereunder at the rates or in the amounts specified in this Agreement, provided that the Company shall not be obligated to pay such amounts with respect to any period in

which the Bank has failed (x) to file any form or certificate that it was entitled to file which would have exempted the Bank from such Taxes or (y) to take other action which would entitle the Bank to an exemption from such Taxes, if such action would not, in the reasonable judgement of the Bank, be otherwise disadvantageous to it. Whenever any Tax is payable by the Company, as promptly as possible thereafter, the Company shall send the Bank a receipt or other evidence of payment thereof.

(iv) A certificate as to the nature of the occurrence giving rise to, and the calculation of, compensation to the Bank pursuant to clauses (i), (ii) and (iii) of this Section 2(c) above shall be submitted by the Bank to the Company and shall be conclusive (absent demonstrable error) as to the amount thereof.

(v) The Company agrees that its obligations to pay compensation pursuant to this Section 2(c) shall inure to the benefit of each Participant and each Successor Participant with respect to its respective participation to the same extent as if such Participant or Successor Participant were named instead of the Bank in this Section 2(c), provided that any certificate presented by the Bank on behalf of a Participant or Successor Participant pursuant to Section 2(c)(iv) hereof shall provide the identity of such Participant or Successor Participant and an estimate of the total additional compensation which would be payable to such Participant or Successor Participant on an annual basis.

(vi) No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which the Bank is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by the Bank. No law, rule or regulation in the form in which it is in effect on the Date of Issuance, but excluding changes in the interpretation or administration thereof after the Date of Issuance, or Tax to which a Participant is subject on the Date of Issuance shall be used as the basis of a claim for compensation pursuant to Section 2(c) by such Participant.

(d) All payments by the Company to the Bank under this Section 2 shall be made in lawful currency of the United States and in immediately available funds at the Bank's principal New York office, which at the date hereof is located at 23 Wall Street, New York, New York 10015, provided that the fee payable under the last sentence of Section 2(b) may be

paid in New York Clearinghouse Funds. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding Business Day, and any interest payable thereon shall be payable for such extended time at the specified rate.

(e) Interest payable under subsection (a) and the fees payable under subsection (b) shall be computed on the basis of a year of 365 days (or 366 days in a leap year) and paid for the actual number of days lapsed (including the first day but excluding the last day).

SECTION 3. Issuance of the Letter of Credit; Conditions Precedent to Issuance. (a) Subject to satisfaction of the conditions precedent set forth in subsections (b), (c) and (d) of this Section, the Bank shall issue the Letter of Credit on the date set forth in the notice referred to in section 3(b)(viii) hereof (such date or such later date on which the conditions precedent are satisfied and the Letter of Credit is issued being herein called the "Date of Issuance"). The Letter of Credit shall be effective on the Date of Issuance and shall expire on the Termination Date.

(b) As a condition precedent to the issuance of the Letter of Credit, the Bank shall have received on or before the Date of Issuance the following, each dated such date, in form and substance satisfactory to the Bank:

(i) opinions of Snell & Wilmer, counsel for the Company, substantially in the form of Exhibit B hereto;

(ii) opinions of Mudge Rose Guthrie Alexander & Ferdon, special counsel for the Company, substantially in the form of Exhibit C hereto;

(iii) an opinion of Davis Polk & Wardwell, counsel for the Bank, substantially in the form of Exhibit D hereto;

(iv) copies of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance by the Company of this Agreement, each of the Transaction Documents to which the Company is a party and the Collateral Trust Indenture, certified by the Secretary, an Assistant Secretary or an Associate Secretary of the Company (which certificate shall state that such

resolutions are in full force and effect on the Date of Issuance);

(v) certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency required for the Company to enter into this Agreement and of all such approvals, authorizations, orders, consents, notices or registrations required to be obtained or made prior to the Date of Issuance in connection with the transactions contemplated by any of the Transaction Documents or Financing Documents to which the Company is a party;

(vi) a certificate of the Secretary, an Assistant Secretary or an Associate Secretary of the Company certifying the names and true signatures of the officers of the Company authorized to sign this Agreement and the other documents to be delivered by the Company hereunder;

(vii) such other documents, instruments, approvals (and, if requested by the Bank, certified duplicates of executed copies thereof) or opinions as the Bank may reasonably request in writing; and

(viii) receipt by the Bank of a written notice of the proposed Date of Issuance signed by the Company and the Equity Participant.

(c) The following statements shall be true and correct on the Date of Issuance and the Bank shall have received a certificate signed by a duly authorized officer of the Company, dated the Date of Issuance, stating that:

(i) the representations and warranties contained in Section 6 hereof are correct on and as of the Date of Issuance as though made on and as of such date; and

(ii) no Default shall have occurred and be continuing and no Default shall result from the issuance of the Letter of Credit.

(d) On or before the Date of Issuance,

(i) each of the Transaction Documents shall have been duly authorized and executed by the respective parties thereto and shall be in full force and effect;

(ii) the Bank shall have received executed copies (or duplicates thereof) of each Transaction Document, each of which shall be in form and substance satisfactory to the Bank;

(iii) all conditions precedent to the Closing set forth in Section 5(b) of the Participation Agreement shall have been fulfilled; and

(iv) the Purchase Documents shall have been delivered to the Owner Trustee.

SECTION 4. Adjustment of Maximum Drawing Amount; Terms of Drawing. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

SECTION 5. Obligations Absolute. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement, under all circumstances whatsoever, including without limitation the following circumstances:

(a) any lack of validity or enforceability of the Letter of Credit or any of the Transaction Documents or Financing Documents;

(b) any amendment or waiver of or any consent to departure from all or any of the Transaction Documents or Financing Documents;

(c) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant or the Owner Trustee (or any persons or entities for whom any of the foregoing may be acting), the Bank or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents or any unrelated transactions, provided that nothing herein shall prevent the

assertion of any such claim by separate suit or compulsory counterclaim;

(d) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(e) payment by the Bank under the Letter of Credit against presentation of a draft or certificate which does not comply with the terms of such Letter of Credit; or

(f) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

SECTION 6. Representations and Warranties. The Company represents and warrants as follows:

(a) Corporate Existence and Power. The Company is a corporation duly incorporated, validly existing and in good standing under the laws of the State of Arizona, is duly qualified to do business in and is in good standing under the laws of the State of New Mexico and has all corporate powers and all material governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted. All of the issued and outstanding common stock of the Company is owned by AZP Group, Inc.

(b) Corporate Authorization. The execution, delivery and performance by the Company of this Agreement and each Transaction Document and Financing Document (except, for purposes hereof, the Underwriting Agreement) to which it is, or is to become, a party, have been duly authorized by all necessary corporate action on the part of the Company and do not, and will not, require the consent or approval of AZP Group, Inc. or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been, or on or before the Date of Issuance, in the case of the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan, will have been, duly obtained, given or accomplished.

(c) No Violation, etc. Neither the execution, delivery or performance by the Company of this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, nor the consummation by the Company

of the transactions contemplated hereby or thereby, nor compliance by the Company with the provisions hereof or thereof, conflicts or will conflict with, or results or will result in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any indenture, mortgage, lease or any other agreement or instrument to which the Company or any Affiliate of the Company is a party or by which the property of the Company or any Affiliate of the Company is bound, or results or will result in the creation or imposition of any Lien (other than Permitted Liens) upon any property of the Company or any Affiliate of the Company. There is no provision of the Restated Articles of Incorporation or Bylaws of the Company, or any Applicable Law, or any such indenture, mortgage, lease or other agreement or instrument which materially adversely affects, or in the future is likely (so far as the Company can now foresee) to materially adversely affect, the business, operations, affairs, condition, properties or assets of the Company, or its ability to perform its obligations under this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party.

(d) Governmental Actions. No Governmental Action under any Federal, Arizona or New York law is or will be required in connection with the execution, delivery or performance by the Company of, or the consummation by the Company of the transactions contemplated by, this Agreement or any Transaction Document or Financing Document to which it is, or is to become, a party, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of the Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required under existing Federal, Arizona or New York law to be obtained, given or accomplished from time to time after the Date of Issuance in connection with the maintenance, use, possession or operation of Unit 2 or otherwise with respect to Unit 2 and the Company's or the Operating Agent's involvement therewith and which are, for PVNGS, routine in nature and which the Company has no reason to believe will not be timely obtained and (iii) as may be required under Applicable Law not now in effect. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required (a) in

connection with the participation by the Bank or any Participant in the consummation of the transactions contemplated by this Agreement, or in connection with the participation by the Owner Trustee, the Indenture Trustee, the Equity Participant, Funding Corp. or any Loan Participant in the consummation of the transactions contemplated by the Transaction Documents or Financing Documents or (b) to be obtained by any of such Persons during the Lease Term, except such Governmental Actions (i) as have been, or on or before the Date of Issuance, in the case of this Agreement and the Transaction Documents, or the Refunding Date, in the case of any Refunding Loan or any Financing Documents, will have been, duly obtained, given or accomplished, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of any obligations issued under and pursuant to any Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required by existing Applicable Law if, after the Lease Termination Date, the Company should redeliver the Undivided Interest to the Owner Trustee pursuant to Section 16(a) of the Facility Lease or provide transmission services for the Owner Trustee and sell the Retained Assets to the Owner Trustee as provided under the Assignment and Assumption, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person under Section 16 of the Facility Lease.

(e) Execution and Delivery. This Agreement and the Transaction Documents to which the Company is, or is to become, a party on or prior to the Date of Issuance have been or on or before the Date of Issuance will have been duly executed and delivered by the Company, and this Agreement is and upon execution and delivery thereof each such Transaction Document will be the legal, valid and binding obligations of the Company in accordance with their respective terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(f) Litigation. There is no pending action or proceeding before any court, governmental agency or arbitrator against or directly involving the Company or any of its Sub-

subsidiaries and, to the best of the Company's knowledge, there is no pending or threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator (A) in which any question is raised as to the validity of this Agreement or any of the Transaction Documents or Financing Documents, or (B) (except as set forth in (i) the Company's Report on Form 10-K for the fiscal year ended December 31, 1985 (the "1985 Form 10-K") in Item 1 thereof under "Rates-State", and "Environmental Requirements", "Generating Fuel", "Water Supply" and "Indian Matters" or in Item 2 thereof, (ii) the Company's Report on Form 10-Q for the fiscal quarter ended March 31, 1986 in Item 5 thereof under "Retail Rates", "Palo Verde Nuclear Generating Station" and "Environmental Requirements" and (iii) the Company's Report on Form 10-Q for the fiscal quarter ended June 30, 1986 in Item 1 thereof under "Water Supply" and in Item 5 thereof under "Retail Rates" and "Palo Verde Nuclear Generating Station") in which there is any material likelihood of an outcome which may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents. There has been no determination (interim or final) in any action or proceeding so disclosed which determination may materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents.

(g) Material Adverse Change. The consolidated balance sheet of the Company and its Consolidated Subsidiaries as at December 31, 1985, and the related consolidated statements of income, of retained earnings and of changes in financial position of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Bank, present fairly the financial position of the Company and its Consolidated Subsidiaries as at such date and the results of the operations of the Company and its Consolidated Subsidiaries for the year ended on such date, in accordance with generally accepted accounting principles consistently applied, and since December 31, 1985, there has been no material adverse change in such position or operations, except as set forth in Appendix A hereto.

(h) Compliance with ERISA. The Company and each member of the Controlled Group have fulfilled their obligations under the minimum funding standards of ERISA and the Code with respect to each Plan (or, with respect to each Plan which is a multiemployer plan as defined in Section 4001(a)(3) of ERISA, have made all required contributions), are in compliance (other than any instance of non-compliance

the liability for which is not material to the Company's or Controlled Group's financial condition) with the presently applicable provisions of ERISA and the Code, and no events have occurred which have or could result in the imposition of any liability to the PBGC or a Plan under Title IV of ERISA.

SECTION 7. Affirmative Covenants. The Company agrees that during the term of this Agreement it will:

(a) Preservation of Corporate Existence, Etc. (i) Preserve and maintain its corporate existence in the state of its incorporation and qualify and remain qualified as a foreign corporation in each jurisdiction in which such qualification is reasonably necessary in view of its business and operations or the ownership of its properties and (ii) preserve, renew and keep in full force and effect the rights, privileges and franchises necessary or desirable in the normal conduct of its business, except that (a) the Company from time to time makes minor extensions of its system prior to the time a related franchise, certificate, license, or permit is procured, (b) from time to time communities already being served by the Company become incorporated and considerable time may elapse before a franchise is procured, (c) certain franchises may have expired prior to the renegotiation thereof, (d) the Company may not have obtained certain permits or variances relating to the environmental requirements prescribed under "Environmental Requirements" in Item 1 in the 1985 Form 10-K and (e) certain minor defects and exceptions may exist which, individually and in the aggregate, are not deemed material.

(b) Compliance with Laws, Etc. Use its best efforts to comply, and use its best efforts to cause each of its Material Subsidiaries to comply, in all material respects with all applicable laws, rules, regulations, and orders of any governmental authority, the non-compliance with which would materially and adversely affect the business or condition of the Company and its Material Subsidiaries, taken as a whole, such compliance to include, without limitation, paying before the same become delinquent all material taxes, assessments and governmental charges imposed upon it or upon its property, except to the extent compliance with any of the foregoing is then being contested in good faith.

(c) Maintenance of Insurance, Etc. Maintain insurance with responsible and reputable insurance companies or associations or through its own program of self-insurance in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar

properties in the same general areas in which the Company operates and furnish to the Bank within a reasonable time after written request therefor, such information as to the insurance carried as the Bank may reasonably request.

(d) Visitation Rights. At any reasonable time and from time to time, permit the Bank or any agents or representatives thereof to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; provided, however, that the Company reserves the right to restrict access to any of its generating facilities in accordance with reasonably adopted procedures relating to safety and security; and provided, further, that, Section 18 hereof notwithstanding, the costs and expenses incurred by the Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions occurring or made prior to the occurrence of an Event of Default shall be for the account of the Bank. The Bank agrees to use reasonable efforts to ensure that any information concerning the Company or any of its Subsidiaries obtained by the Bank pursuant to this Section which is not contained in a report or other document filed with the Securities and Exchange Commission, distributed by the Company to its security holders or otherwise generally available to the public will, to the extent permitted by law and except as may be required by valid subpoena or in the normal course of the Bank's business operations (which shall include the Bank's sharing of its liability under the Letter of Credit with other banks), be treated confidentially by the Bank and will not be distributed or otherwise made available by the Bank to any Person, other than the Bank's employees, authorized agents or representatives.

(e) Keeping of Books. Keep, and cause each Material Subsidiary to keep, proper books of record and account, in which entries shall be made of all financial transactions and the assets and business of the Company and each Material Subsidiary in accordance with generally accepted accounting principles.

(f) Maintenance of Properties. Maintain and preserve, and cause each Material Subsidiary to maintain and preserve, all of its properties which are used or which are useful in the conduct of its business in good working order and condition, ordinary wear and tear excepted, it being understood that this covenant relates only to the good working

order and condition of such properties and shall not be construed as a covenant of the Company or any Material Subsidiary not to dispose of such properties by sale, lease, transfer or otherwise.

(g) Reporting Requirements. Furnish to the Bank the following: (i) as soon as practicable, and in any event within ten days after the Company knows or has reason to know of the occurrence of a Reimbursement Default which is continuing on the date of such statement, a statement of the chief financial officer (or in his absence, a principal financial officer) of the Company setting forth details of such Reimbursement Default and the action which the Company proposes to take with respect thereto; (ii) as soon as available and in any event within 15 days after filing of each of the Company's Reports on Form 8-K with the Securities and Exchange Commission, a copy of each such report; (iii) as soon as available and in any event within 30 days after filing of each of the Company's Reports on Form 10-Q with the Securities and Exchange Commission, a copy of each such report together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company stating (x) that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (iv) as soon as available and in any event within 30 days after filing of each of the Company's Annual Reports on Form 10-K with the Securities and Exchange Commission, a copy of each such report, together with a certificate of the chief financial officer (or in his absence, a principal financial officer) of the Company (x) stating that no Reimbursement Default has occurred and is continuing or, if a Reimbursement Default has occurred and is continuing, a statement as to the nature thereof and the action which the Company proposes to take with respect thereto and (y) setting forth in reasonable detail the calculations required to establish whether the Company was in compliance with the requirements of Section 7(i) hereof on the date of the consolidated balance sheet contained in such report; (v) as soon as available and in any event within 20 days after any member of the Controlled Group (x) gives or is required to give notice to the PBGC of any "reportable event" (as defined in Section 4043 of ERISA) with respect to any Plan which might constitute grounds for the termination of such Plan under Title IV of ERISA, or knows

that the plan administrator of any Plan has given or is required to give notice of any such reportable event, a copy of the notice of such reportable event given or required to be given to the PBGC, provided that no such information need be given with respect to any reportable event for which the 30-day notice requirement of Section 4043(a) of ERISA has been waived, (y) receives notice of complete or partial withdrawal liability under Title IV of ERISA, a copy of such notice or (z) receives notice from the PBGC under the Title IV of ERISA of an intent to terminate or appoint a trustee to administer any Plan, a copy of such notice, (vi) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the Transaction Documents and Financing Documents and (vii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the Company as the Bank may from time to time reasonably request in writing.

(h) Maintenance of Equity. Maintain at all times consolidated common stockholders equity, as calculated in accordance with generally accepted accounting principles consistently applied, of at least \$1.4 billion.

(i) Fixed Charge Ratio. Maintain at all times a Fixed Charge Ratio of at least 2 to 1. "Fixed Charge Ratio" shall mean at any time the ratio of (A) the sum of (x) the consolidated net income of the Company and its Consolidated Subsidiaries for the twelve month period ending with the last month for which the Company has prepared a consolidated income statement, which period shall in no event end earlier than the last day of the month two months prior to the time of the calculation of the Fixed Charge Ratio (the "Twelve Month Period") plus (y) all income taxes deducted in determining said consolidated net income plus (z) the sum of (i) all interest expense in respect of Indebtedness deducted in determining said consolidated net income, (ii) all interest expense in respect of Funded Indebtedness being incurred at the time of calculation of the Fixed Charge Ratio that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate and (iii) all interest expense in respect of Indebtedness other than Funded Indebtedness (I) incurred at any time subsequent to the Twelve Month Period outstanding at the time of the calculation of the Fixed Charge Ratio and (II) being incurred at the time of the calculation of the Fixed Charge Ratio, that would have been payable if such Indebtedness had been outstanding during the Twelve Month Period accruing interest at the Imputed Rate, (iv) to the extent not covered under clauses

(i), (ii) or (iii) above, (I) rentals payable under Operating Lease Obligations during the Twelve Month Period and (II) with respect to Operating Lease Obligations entered into subsequent to the Twelve Month Period or being entered into at the time of calculation of the Fixed Charge Ratio, the rentals that would have been payable if such Operating Lease Obligations had been outstanding during the Twelve Month Period, provided that rentals payable under any Operating Lease Obligation shall not be included in the calculation of the Fixed Charge Ratio under this clause (iv) until the date that is nine months after the first day of the lease term of such Operating Lease Obligation (the aggregate interest expense and rental payments described in this clause (2) being referred to as the "Interest Expense") to (B) Interest Expense for such period.

SECTION 8. Negative Covenants. The Company agrees that, during the term of this Agreement it will not:

(a) Sales, Etc. of Assets. Sell, lease, transfer or otherwise dispose of (or pledge or otherwise encumber), in any one fiscal year in one or a series of transactions to one or more Persons, including any Subsidiary or Affiliate of the Company, assets with an aggregate value exceeding 10% of the value of the assets of the Company as shown on the consolidated balance sheet of the Company and its Consolidated Subsidiaries included in its audited financial statements for its most recent fiscal year, such assets to be valued on the same basis as that on which they were included in such consolidated financial statements, or, if such assets were not included in such consolidated financial statements, on the same basis as similar assets were valued for such consolidated financial statements, provided, however, that the Company may (i) pledge or encumber assets in connection with the sale of bonds issued under the Company Indenture, (ii) enter into sale and sale-back and sale and lease-back arrangements in connection with Unleased Interests and (iii) create or suffer to exist Excepted Encumbrances as defined in the Company Indenture.

(b) Mergers, Etc. Merge with or into or consolidate with or into any other corporation or entity, or permit any Subsidiary to do so unless (i) immediately after giving effect thereto, no event shall occur and be continuing which constitutes a Reimbursement Default, (ii) the consolidation or merger shall not materially and adversely affect the ability of the Company to perform its obligations hereunder or under any of the Transaction Documents or Financing Documents and (iii) in the case of any merger or consolidation to which the Company is a party, the corporation

formed by such consolidation or into which the Company shall be merged shall assume the Company's obligations under this Agreement in a writing satisfactory in form and substance to the Bank.

(c) Compliance with ERISA. (i) Enter into any prohibited transaction (as defined in Section 4975 of the Internal Revenue Code of 1954, as amended, and in ERISA) involving any Plan which results in any liability of the Company to any Person which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company or (ii) allow or suffer to exist any other event or condition known to the Company which results in any liability of the Company to the PBGC which (in the reasonable opinion of the Bank) is material to the financial position or operations of the Company. For purposes of this Section 8(c), "liability" shall not include the contingent liability described in Sections 4201 and 4062 of ERISA or termination insurance premiums payable under Section 4007 of ERISA.

(d) Assignment of Transaction Documents or Financing Documents. After the Date of Issuance, enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents, without first obtaining the express prior written consent of the Bank thereto.

SECTION 9. Reimbursement Events of Default. The following events shall be Reimbursement Events of Default hereunder unless waived by the Bank pursuant to Section 10 hereof:

(i) the Company shall fail to pay when due any amount payable under Section 2 hereunder; or

(ii) the Company shall fail to observe or perform any covenant or agreement contained in this Agreement (other than those covered by clause (i) above or Sections 7(d) and 18 hereof) for 30 days after written notice thereof has been given to the Company by the Bank; or

(iii) any representation, warranty, certification or statement made by the Company in this Agreement or in any certificate, financial statement or other document delivered pursuant to this Agreement shall prove to have been incorrect in any material respect when made; or

(iv) any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) the Company shall (x) fail to make any payment, equal to or exceeding \$5,000,000 of any Outstanding Debt, or to make any payment, equal to or exceeding \$5,000,000, of any interest or premium thereon, when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument relating to the Outstanding Debt, or (y) fail to perform or observe any other term, covenant or condition on its part to be performed or observed under any agreement or instrument relating to any Outstanding Debt when required to be performed or observed, and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure to perform or observe is to accelerate, or to permit the acceleration of, the maturity of any Outstanding Debt, the unpaid principal amount of which then equals or exceeds \$5,000,000; or.

(vi) the Company shall (A) apply for or consent to the appointment of a receiver, trustee, liquidator or custodian or the like of itself or of its property, (B) admit in writing its inability to pay its debts generally as they become due, (C) make a general assignment for the benefit of creditors, (D) be adjudicated a bankrupt or insolvent, or (E) commence a voluntary case under the Federal bankruptcy laws of the United States of America or file a voluntary petition or answer seeking reorganization, an arrangement with creditors or any order for relief or seeking to take advantage of any insolvency law or file an answer admitting the material allegations of a petition filed against it in any bankruptcy, reorganization or insolvency proceeding; or corporate action shall be taken by it for the purpose of effecting any of the foregoing, or if without the application, approval or consent

of the Company, a proceeding shall be instituted in any court of competent jurisdiction, seeking in respect of the Company an adjudication in bankruptcy, reorganization, dissolution, winding up, liquidation, a composition or arrangement with creditors, a readjustment of debts, the appointment of a trustee, receiver, liquidator or custodian or the like of the Company or of all or any substantial part of its assets, or other like relief in respect thereof under any bankruptcy or insolvency law, and, if such proceeding is being contested by the Company in good faith, the same shall (i) result in the entry of an order for relief of any such adjudication or appointment or (ii) continue undismissed, or pending and unstayed, for any period of seventy-five (75) consecutive days; or

(vii) any judgment or order for the payment of money exceeding any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and either (i) enforcement proceedings shall have been commenced by any creditor upon such judgment or order or (ii) there shall be any period of ten consecutive days during which a stay of enforcement of such judgment or order, by reason of a pending appeal or otherwise, shall not be in effect; or

(viii) the Company or any member of the Controlled Group shall fail to pay when due an amount or amounts aggregating in excess of \$5,000,000 which it shall have become liable to pay to the PBGC or to a Plan under Title IV of ERISA; or notice of intent to terminate a Plan or Plans having aggregate Unfunded Vested Liabilities in excess of \$10,000,000 (collectively a "Material Plan") shall be filed under Title IV of ERISA by the Company, any member of the Controlled Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate or to cause a trustee to be appointed to administer any Material Plan; or a proceeding shall be instituted by a fiduciary of any Material Plan against the Company or any member of the Controlled Group to enforce Section 515 of ERISA in which the amount in controversy exceeds \$1,000,000 and such proceeding shall not have been dismissed within 30 days thereafter; or a condition shall exist by reason of which the PBGC would be entitled under

Title IV of ERISA to obtain a decree adjudicating that any Material Plan must be terminated; or

(ix) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(x) any event specified in Sections 15 (vii), (viii) or (x) of the Facility Lease shall occur; or

(xi) the Company shall fail to make, or cause to be made, any payment specified in Section 15 (i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

If an Event of Default occurs and is continuing, the Bank may, in its sole discretion by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein.

SECTION 10. Amendments and Waivers. No amendment or waiver of any provision of this Agreement, nor consent to any departure by the Company therefrom nor any consent to the assignment of the Company's obligations under the Transaction Documents or the Financing Documents shall in any event be effective unless the same shall be in writing and signed by the Bank. Any such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given.

SECTION 11. Notices. All notices, requests and other communications to any party hereunder shall be in writing (including telex or similar writing) and shall be given to such party, addressed to it, at its address or telex number set forth below or such other address or telex number as such party may hereafter specify for the purpose by notice to the other party. Each such notice, request or communication shall be effective (i) if given by telex, when such telex is transmitted to the telex number specified below and the appropriate answerback is received, (ii) if given by mail upon receipt but not later than 10 days after such communication is deposited in the mails with first class postage prepaid, addressed as aforesaid or (iii) if given by any other means, when delivered at the address specified below.

Party
Arizona Public Service
Company

Address
Street Address:
411 North Central Avenue
Phoenix, Arizona 85004

Mailing Address:

P.O. Box 53999
Phoenix, Arizona 85072-3999
Attention: Treasurer
Telex: TWX165232
Answerback: APS PHNX
Facsimile Transmission:
(602) 250-2061

Morgan Guaranty Trust
Company of New York

150 William Street
17th Floor
New York, New York 10015
Attn: Letter of Credit
Department
(Copy to
Utilities Department)
Telex: 420230
Answerback: MGT UI
or
Telex: 232194
Answerback: MGT UR
Facsimile Transmission:
(212) 344-9454

SECTION 12. No Waiver; Remedies. No failure on the part of the Bank to exercise, and no delay in exercising, any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise of any right hereunder preclude any other further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

SECTION 13. Waiver of Right of Setoff. The Bank hereby waives any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by the Bank to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up,

reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "bankruptcy events"), against any and all of the obligations of the Company now or hereafter existing in respect of the reimbursement obligation of the Company set forth in Section 2(a) hereof, provided any such waiver shall be deemed ineffective as and to the extent that the Bank receives, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience, (which counsel shall be mutually satisfactory to the Bank and the Owner Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section.

SECTION 14. Sales of Participations. The Bank may grant participations under this Agreement and the Letters of Credit (each person to which a participation is granted being called a "Participant") and in such event the Bank will in its own name and as agent for any Participant, enforce all rights and interests of any Participant under this Agreement, and accept all performances required of the Company under this Agreement, provided that (i) the Bank shall not agree to a substitution or replacement of a Participant or a change in the proportionate amount of any Participant's participation after the Date of Issuance unless the Bank shall have received the Company's prior written consent thereto, which consent shall not be unreasonably withheld and (ii) in the event that a claim for compensation is made pursuant to Section 2(c) on behalf of a Participant, the Company shall have the right, with the assistance of the Bank, to seek a substitute participant or participants, satisfactory to the Bank, to assume the participation of such Participant.

SECTION 15. Continuing Obligation. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date or (ii) the date upon which all amounts due and owing to the Bank hereunder shall have been paid in full and shall (a) be binding upon the Company

and its successors and assigns and (b) inure to the benefit of and be enforceable by the Bank and its successors, transferees and assigns, provided, however, that the Company may not assign all or any part of this Agreement without the prior written consent of the Bank.

SECTION 16. Extension of Letter of Credit. At least 90 but not more than 180 days before the fifth anniversary of the Date of Issuance, the Company may request the Bank in writing to extend for not less than three years, nor more than eight years, the Termination Date of the Letter of Credit, specifying the terms and conditions, including fees, to be applicable to such extension. No later than 30 days from the date on which the Bank shall have received notice from the Company pursuant to the preceding sentence, the Bank shall notify the Company of its consent or nonconsent to such extension request, and if the Bank shall give no such notice, the Bank shall be deemed not to have consented to such extension request. The Bank's consent shall be conditional upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to the Bank and its counsel incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement between the Company and the Bank.

SECTION 17. Limited Liability of the Bank. The Company assumes all risks of the acts or omissions of the Equity Participant with respect to its use of the Letter of Credit. Neither the Bank nor any of its officers or directors shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or for any acts or omissions of the Equity Participant in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement(s) thereon, even if such documents should in fact prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except only that the Company shall have a claim against the Bank, and the Bank shall be liable to the Company to the extent, but only to the extent, of any direct, as opposed to consequential, damages suffered by the Company which the Company proves were caused by (i) the Bank's willful misconduct or gross negligence in determining whether documents presented under the Letter of Credit comply with the terms thereof or (ii) the Bank's willful failure to pay under the Letter of Credit after the

presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. In furtherance and not in limitation of the foregoing, the Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

SECTION 18. Costs, Expenses and Taxes. The Company agrees to pay not later than 30 days after demand therefor all reasonable costs and expenses in connection with the preparation, execution, delivery, filing and administration of this Agreement and any other documents which may be delivered in connection with this Agreement, including, without limitation, the reasonable fees and out-of-pocket expenses of counsel for the Bank with respect thereto and with respect to advising the Bank as to its rights and responsibilities under this Agreement or any waiver or amendment of, or the enforcement of, this Agreement and such other documents which may be delivered in connection with this Agreement. In addition, the Company shall pay any and all stamp and other taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents and agrees to save the Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, provided that the Bank agrees promptly to notify the Company of any such taxes and fees which are incurred by the Bank.

SECTION 19. Indemnification. The Company hereby agrees to indemnify and hold harmless the Bank from and against any and all claims, damages, losses, liabilities, costs or expenses whatsoever which the Bank may incur (or which may be claimed against the Bank by any person or entity whatsoever) (i) by reason of any inaccuracy in any material respect, or untrue statement or alleged untrue statement of any material fact contained or incorporated by reference in any offering document distributed by or on behalf of the Company in connection with obtaining purchasers of the Company's undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station, or in any supplement or amendment to either thereof, or the omission or alleged omission to state therein a material fact necessary to make such statements, in the light of the circumstances under which they are or were made, not misleading; (ii) by reason of or in connection with

the execution, delivery and performance of the Transaction Documents and Financing Documents; or (iii) by reason of or in connection with the execution and delivery or transfer of, or payment or failure to make lawful payment under, the Letter of Credit; provided that the Company shall not be required to indemnify the Bank for any claims, damages, losses, liabilities, costs or expenses to the extent, but only to the extent, caused by the willful misconduct or gross negligence of the Bank in determining whether a draft or certificate presented under the Letter of Credit complied with the terms of the Letter of Credit or the Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. Nothing in this Section 19 is intended to limit the Company's reimbursement obligation contained in paragraph (a) of Section 2 hereof. Without prejudice to the survival of any other obligation of the Company hereunder, the indemnitees and obligations of the Company contained in this Section 19 shall survive the payment in full of amounts payable under Section 2 and the termination of the Letter of Credit.

SECTION 20. Severability. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

SECTION 21. Governing Law. This Agreement shall be governed by, and construed and interpreted in accordance with, the laws of the State of New York.

SECTION 22. Headings. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By _____
Title:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK

By _____
Title:

IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. S-1002

August 18, 1986

Emerson Finance Co.
111 Prospect Street
Stamford, Connecticut 06901

Attn: President

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "Company"), in your favor, our Irrevocable Transferable Letter of Credit No: S-1002 (the "Letter of Credit"), in an amount not to exceed \$69,493,938.93 (the "Maximum Credit Amount"), effective immediately and expiring at 5:00 p.m. (New York time) on the Termination Date. Capitalized terms used herein and in Schedules II and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "Facility Lease") between the Company and the First National Bank of Boston, as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "Date of Drawing") in the Table of Maximum Drawing Amounts attached hereto as Schedule II as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next paragraph, are hereinafter referred to collectively as the "Maximum Drawing Amounts" and individually as the "Maximum Drawing Amount". A drawing in respect of a payment hereunder honored by us shall not exceed

the lesser of the Maximum Drawing Amount applicable on the Date of Drawing and the Maximum Credit Amount.

The Maximum Drawing Amounts shall be modified from time to time as follows:

(a) upon payment by the Bank of each drawing under the Letter of Credit, the Maximum Drawing Amounts applicable to each Date of Drawing subsequent to such payment shall be automatically reduced by an amount equal to the amount of the drawing so paid and shall not be reinstated; and

(b) if adjustments are made to Modified Special Casualty Values, corresponding adjustments shall be made to the Maximum Drawing Amounts shown in Schedule II, (as theretofor reduced pursuant to clause (a) above), provided that if any such adjustment of Modified Special Casualty Values would cause the Maximum Drawing Amount for any period to exceed the Maximum Credit Amount, the Maximum Credit Amount shall apply for such period and provided further that adjustments pursuant to this clause (b) shall be effective automatically upon receipt by us of a notice from you in the form of Exhibit 1 hereto.

Upon surrender of this Letter of Credit together with a notice in the form of Exhibit 1 hereto, we will promptly issue an irrevocable transferable letter of credit containing a revised Schedule II reflecting the adjustments contained in such notice and in all other respects identical to this Letter of Credit.

Funds under this Letter of Credit are available to you against presentation on or prior to the Termination Date of (a) your draft in the form of Exhibit 2 attached hereto and (b) a completed certificate signed by you in the form of Exhibit 3 attached hereto. Such draft and certificate shall be dated the date of presentation and shall be made at our office located at 23 Wall Street, New York New York 10015, Attention: Letter of Credit Department (or at any other office in the City and State of New York which may be designated by us by written notice (given in the manner set forth in the next paragraph) delivered to you at least 15 days prior to the applicable Date of Drawing). If we receive such draft and certificate at such office, all in strict conformity with the terms and conditions of this Letter of Credit, prior to 10:00 a.m. (New York time) on any Business Day, we will honor the draft on the same Business Day. If we receive such draft and certificate at such office, all in strict conformity with the terms and conditions of this Letter of Credit, on or after 10:00 a.m. (New York time) on any Business Day, we will honor the draft on the next Business Day. If requested by you, payment under this Letter

of Credit may be made by wire transfer of federal funds to your account with any bank located in the United States of America or by deposit of immediately available funds into a designated account that you maintain with us.

Notwithstanding any other provision of this Letter of Credit, we shall have the right, upon the occurrence of any of the events listed in Schedule III hereto, to terminate this Letter of Credit by delivering to you a written notice indicating the date of such termination (the "Date of Early Termination"), provided that on or before the Date of Early Termination you will have the right to draw once an amount not in excess of the Maximum Drawing Amount in accordance with the procedures described herein. The written notice referred to in the preceding sentence shall be given by telex or facsimile transmission addressed to you at Emerson Finance Co., 111 Prospect Street, Stamford, Connecticut 06901, Attention: President (or to such other address or telex number designated by you by written notice delivered to us at least 15 days prior to the notice of early termination) and shall be effective upon receipt of the appropriate answerback or confirmation of the facsimile transmission. We will also forward a copy of such notice by overnight delivery service to the address set forth above. The Date of Early Termination specified in such written notice shall be:

(a) in the case of events specified in paragraphs A and F of Schedule III, not earlier than ten days after such notice is given, and

(b) in the case of all other events specified in Schedule III, not earlier than 30 days after such notice is given.

Except as set forth below, this Letter of Credit shall be governed by the Uniform Customs and Practice for Documentary Credits (revision effective October 1, 1984) International Chamber of Commerce Publication No. 400, and, as to matters not covered therein, be governed by the laws of the State of New York, including without limitation the Uniform Commercial Code as in effect in such State. Communications with respect to this Letter of Credit shall be in writing and shall be addressed to us at 23 Wall Street, New York, New York 10015, Attention: Letter of Credit Department (with a copy to Utilities Department) and shall specifically refer to the number of this Letter of Credit.

Notwithstanding Article 54 of the Uniform Customs and Practice for Documentary Credits referred to above, this Letter of Credit may be transferred and assigned in its entirety more than once, but in each case only to the successor Owner Par-

participant under the Trust Agreement dated as of August 1, 1986 between yourself and the First National Bank of Boston. Upon receipt by us at the address for presentation of documents set forth above of a copy of the instrument effecting such transfer and assignment, signed by the transferor and by the transferee, in the form of Exhibit 4 hereto (which shall be conclusive evidence of such assignee's authority without any inquiry by us into the terms of the Trust Agreement) then, in such case, we will, upon surrender of this Letter of Credit, issue an irrevocable transferable letter of credit in the name of the transferee and providing for notices to be sent to the transferee at the address set forth therein and in all other respects identical to this Letter of Credit and the transferee, instead of the transferor, shall, without necessity of further act, be entitled to all the benefits of, and rights under, this Letter of Credit in the transferor's place.

By your acceptance of this Letter of Credit, you hereby agree, and we hereby confirm our agreement, to the terms and conditions of Section 13 of the Reimbursement Agreement.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein, except only Schedules I, II and III and Exhibits 1, 2, 3 and 4 hereto and the notices referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except as set forth above.

Very truly yours,

MORGAN GUARANTY TRUST
COMPANY OF NEW YORK

By _____
Title:

Morgan Guaranty Trust
Company of New York
23 Wall Street
New York, New York 10015
Attention: Letter of Credit Department

Dear Sirs:

Reference is made to that certain irrevocable transferable Letter of Credit bearing Letter of Credit No. _____ dated [Date of Issuance], which has been established by you in favor of [name of Equity Participant] (the "Equity Participant").

The undersigned, a duly authorized representative of the Equity Participant, hereby certifies that Modified Special Casualty Values have been adjusted and the amounts shown on Schedule II to the Letter of Credit should be modified, in accordance with the terms of clauses (a) and (b) of the third paragraph of the Letter of Credit, to the amounts shown in Appendix A hereto.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit with the revised Schedule II attached and in all other respects identical to the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

[Name of Equity Participant]

[Name and Title of Authorized
Representative of Equity Participant]

EXHIBIT 2

[Place]

[Date] 19

ON [Business Day of presentation if presented before 10:00 a.m.
(New York time); next Business Day if presented after 10:00 a.m.]

PAY TO

[Name of beneficiary]

U.S. \$[not to exceed Maximum
Drawing Amount]
DOLLARS,

FOR VALUE RECEIVED AND CHARGE TO ACCOUNT OF LETTER OF

CREDIT NO. OF

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

[Name and Address of
Equity Participant]

By _____
[Authorized Representative]

CERTIFICATE

The undersigned, a duly authorized representative of [name of Equity Participant] (the "Equity Participant"), as beneficiary under that certain irrevocable transferable Letter of Credit No. _____ dated [the Date of Issuance], established by Morgan Guaranty Trust Company of New York (the "Bank") and issued pursuant to that certain Reimbursement Agreement dated as of August 1, 1986 (the "Reimbursement Agreement") between Arizona Public Service Company (the "Company") and the Bank, hereby certifies as follows:

1. An Event of Default under the Facility Lease has occurred and is continuing.

2. The amount of the accompanying draft does not exceed the Maximum Drawing Amount available under the Letter of Credit on the date hereof, as determined in accordance with the terms of the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed this Certificate as of _____, 19 .

[Name of Equity Participant]

[Name and title of authorized
representative signing certificate]

Organ Guaranty Trust
Company of New York
23 Wall Street
New York, NY 10005

Dear Sirs:

Reference is made to the certain irrevocable transferable Letter of Credit bearing Letter of Credit No. dated [Date of Issuance], which has been established by you in favor of [name of Equity Participant (the "Transferor")].

The Transferor has transferred and assigned (and hereby confirms to you said transfer and assignment) all of its rights in and under said Letter of Credit to [name of Transferee (the "Transferee")] and confirms that the Transferor no longer has any rights under or interest in said Letter Credit.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit in the name of the Transferee and providing for notices to be sent to the Transferee at the address set forth below and in all other respects identical to the Letter of Credit.

Transferee hereby certifies that it is a duly authorized transferee under the terms of said Letter of Credit and is accordingly entitled, upon presentation of the drafts and certificates called for therein, to receive payment thereunder. Notices under the Letter of Credit should be sent to us as follows: [Name], [Address], [Telex Number], Attention: , [Answerback].

[Name of Transferor]

[Name and Title of Authorized
Representative of Transferor]

[Name of Transferee]

[Name and Title of Authorized
Representative of Transferee]

Schedule I

The following terms shall have the following meanings for purposes of the Letter of Credit and the Schedules and Exhibits thereto. Terms defined in the Letter of Credit shall have the meanings given to them therein. Terms defined by reference to the Facility Lease shall have the meanings assigned to them therein from time to time.

"Aggregate Operating Lease Obligations" of any Person means all Operating Lease Obligations under operating leases which are entered into by such Person in substantially contemporaneous transactions.

"Applicable Law" has the meaning assigned to it in the Facility Lease.

"Business Day" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois and the State of California are authorized by law to close.

"Controlled Group" means all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Company, are treated as a single employer under Section 414(b) or 414(c) of Code.

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

"Governmental Action" has the meaning assigned to it in the Facility Lease.

"Modified Special Casualty Value" has the meaning assigned to it in the Facility Lease.

"Operating Lease Obligations" of any Person means all obligations of such Person as lessee under each operating lease of all or a portion of any Unleased Interests.

"Outstanding Debt" of any Person means at any date, without duplication, (i) all obligations of such Person for borrowed money, (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business, (iv) all obligations of such Person as lessee under capital leases, (v) all Aggregate Operating Lease Obligations of such Person, (vi) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, (vii) all Outstanding Debt of others secured by a Lien on any asset of such Person, whether or not such Outstanding Debt is assumed by such Person, and (viii) all obligations, contingent or otherwise, of such Person directly or indirectly guaranteeing any Outstanding Debt of any other Person or in any manner providing for the payment of any Outstanding Debt of any other Person or otherwise protecting the holder of such Outstanding Debt against loss (whether by agreement to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), excluding, however, from this clause (viii) endorsements for collection or deposit in the ordinary course of business.

"PBGC" means the Pension Benefit Guaranty Corporation and any entity succeeding to any or all of its functions under ERISA.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" means at any time an employee pension benefit plan which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Code and is either (i) maintained by a member of the Controlled Group for employees of a member of the Controlled Group or (ii) maintained pursuant to a collective bargaining agreement or any other arrangement under which more than one employer makes contributions and to which a member of the

Controlled Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions.

"Reimbursement Agreement" means the Reimbursement Agreement, dated as of August 1, 1986 between the Company and the Bank as the same may from time to time be amended, supplemented or modified.

"Termination Date" means the earlier of (i) the date on which the Bank pays a drawing under the Letter of Credit for the Maximum Drawing Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Bank pays such drawing, (iv) the date on which the Company pays the amounts due under Section 9(c) of the Facility Lease, (v) the date on which the Company pays the amounts due under Section 9(d) of the Facility Lease or (vi) either (x) the fifth anniversary of the Date of Issuance of the Letter of Credit or (y) if a draft and certificate, all in strict conformity with the terms and conditions of the Letter of Credit, are presented after 10:00 a.m. but prior to 5:00 p.m. (New York time) on the fifth anniversary of the Date of Issuance of the Letter of Credit, the Business Day following such fifth anniversary.

"Transaction Documents" means the Participation Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, the Real Property Interest and the Notes, each as defined in the Facility Lease.

"Unfunded Vested Liabilities" means, with respect to any Plan at any time, the amount (if any) by which (i) the present value of all vested nonforfeitable benefits under such Plan exceeds (ii) the fair market value of all Plan assets allocable to such benefits, all determined as of the then most recent valuation date for such Plan, but only to the extent that such excess represents a potential liability of a member of the Controlled Group to the PBGC or the Plan under Title IV of ERISA.

"Unit 2" has the meaning assigned to it in the Facility Lease.

"Unit 3" means the 1270 megawatt unit, commonly known as Unit 3, at the Palo Verde Nuclear Generating Station, together with all capital improvements thereto.

"Unleased Interests" means any real or personal or mixed property interest of any Person in that portion of Unit 2 and Unit 3 of the Palo Verde Nuclear Generating Station which is not subject to an operating lease immediately after the Letter of Credit has been issued by the Bank.

Schedule II

Table of Maximum Drawing Amounts

<u>Applicable Period</u>	<u>Maximum Drawing Amount</u>
From August 18, 1986 to and including July 10, 1987	\$55,016,068
From July 11, 1987 to and including January 10, 1988	\$60,348,364
From January 11, 1988 to and including July 10, 1988	\$65,220,513
From July 11, 1988 to and including January 10, 1989	\$69,694,224
From January 11, 1989 to and including July 10, 1989	\$73,785,921
From July 11, 1989 to and including January 10, 1990	\$77,557,735
From January 11, 1990 to and including July 10, 1990	\$80,954,364
From July 11, 1990 to and including January 10, 1991	\$83,976,811
From January 11, 1991 to and including July 10, 1991	\$86,565,626
From July 11, 1986 to and including August 18, 1991	\$88,716,898

Schedule III

The Bank shall have the right upon the occurrence of any of the events listed below to terminate the Letter of Credit in accordance with the terms of the Letter of Credit:

(A) the Company shall fail to pay when due any amount payable under Section 2 of the Reimbursement Agreement;

(B) the Company shall fail to observe or perform any covenant or agreement contained in the Reimbursement Agreement (other than those covered by clause (i) above or Sections 7(d) and 18 of the Reimbursement Agreement) for 30 days after written notice thereof has been given to the Company by the Bank;

(C) any representation, warranty, certification or statement made by the Company in the Reimbursement Agreement or in any certificate, financial statement or other document delivered pursuant to the Reimbursement Agreement shall prove to have been incorrect in any material respect when made;

(D) any material provision of the Reimbursement Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under the Reimbursement Agreement;

(E) the Company shall (x) fail to make any payment, equal to or exceeding \$5,000,000 of any Outstanding Debt, or to make any payment, equal to or exceeding \$5,000,000, of any interest or premium thereon, when due (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise) and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument relating to the Outstanding Debt, or (y) fail to perform or observe any other term, covenant or condition on its part to be performed or observed under any agreement or instrument relating to any Outstanding Debt when required to be performed or observed, and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure to perform or observe is to accelerate, or to permit the acceleration of, the maturity of any Outstanding Debt, the unpaid principal amount of which then equals or exceeds \$5,000,000; or

(F) the Company shall (i) apply for or consent to the appointment of a receiver, trustee, liquidator or custodian or the like of itself or of its property, (ii) admit in writing its inability to pay its debts generally as they become due, (iii) make a general assignment for the benefit of creditors, (iv) be adjudicated a bankrupt or insolvent, or (v) commence a voluntary case under the Federal bankruptcy laws of the United States of America or file a voluntary petition or answer seeking reorganization, an arrangement with creditors or any order for relief or seeking to take advantage of any insolvency law or file an answer admitting the material allegations of a petition filed against it in any bankruptcy, reorganization or insolvency proceeding; or corporate action shall be taken by it for the purpose of effecting any of the foregoing, or if without the application, approval or consent of the Company, a proceeding shall be instituted in any court of competent jurisdiction, seeking in respect of the Company an adjudication in bankruptcy, reorganization, dissolution, winding up, liquidation, a composition or arrangement with creditors, a readjustment of debts, the appointment of a trustee, receiver, liquidator or custodian or the like of

the Company or of all or any substantial part of its assets, or other like relief in respect thereof under any bankruptcy or insolvency law, and, if such proceeding is being contested by the Company in good faith, the same shall (a) result in the entry of an order for relief of any such adjudication or appointment or (b) continue undismissed, or pending and unstayed, for any period of seventy-five (75) consecutive days; or

(G) any judgment or order for the payment of money exceeding any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and either (i) enforcement proceedings shall have been commenced by any creditor upon such judgment or order or (ii) there shall be any period of ten consecutive days during which a stay of enforcement of such judgment or order, by reason of a pending appeal or otherwise, shall not be in effect; or

(H) the Company or any member of the Controlled Group shall fail to pay when due an amount or amounts aggregating in excess of \$5,000,000 which it shall have become liable to pay to the PBGC or to a Plan under Title IV of ERISA; or notice of intent to terminate a Plan or Plans having aggregate Unfunded Vested Liabilities in excess of \$10,000,000 (collectively a "Material Plan") shall be filed under Title IV of ERISA by the Company, any member of the Controlled Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate or to cause a trustee to be appointed to administer any Material Plan; or a proceeding shall be instituted by a fiduciary of any Material Plan against the Company or any member of the Controlled Group to enforce Section 515 of ERISA in which the amount in controversy exceeds \$1,000,000 and such proceeding shall not have been dismissed within 30 days thereafter; or a condition shall exist by reason of which the PBGC would be entitled under Title IV of ERISA to obtain a decree adjudicating that any Material Plan must be terminated; or

(I) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by

the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(J) any event specified in Sections 15 (vii), (viii) or (x) of the Facility Lease shall occur; or

(K) the Company shall fail to make, or cause to be made, any payment referred to in Section 15 (i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

EXHIBIT A

ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation hereby certifies the following to Snell & Wilmer in connection with their giving a legal opinion (Legal Opinion) with respect to the sale and leaseback transaction that is the subject matter of the Participation Agreement (Participation Agreement), dated as of August 1, 1986, among the Equity Participant identified on Schedule 1 attached hereto and incorporated herein, PVNGS Funding Corp., Inc., Bank of America National Trust and Savings Association (for itself and as Agent), The First National Bank of Boston (in its individual capacity and as Owner Trustee), Chemical Bank (in its individual capacity and as Indenture Trustee), and APS (all capitalized terms used herein and not otherwise defined herein will have the meanings ascribed to them in the Legal Opinion):

1. The relationship of APS and Owner Trustee in respect of each of the following Transaction Documents intended, agreed to, and understood by APS, Owner Trustee, and each other party to any of the Transaction Documents is as follows:

(a) The relationship of APS and Owner Trustee in respect of the Deed and Bill of Sale and the Assignment and Assumption is one of seller and purchaser, respectively; and

(b) The relationship of Owner Trustee and APS in respect of the Facility Lease is one of lessor and lessee, respectively.

2. Each and all of the operative provisions of the Transaction Documents, in general, and the following basic aspects of the transaction described in and contemplated by the Transaction Documents, in particular, are intended, agreed to, and understood by each and all of APS, Owner Trustee, Equity Participant, and each other party to any of the Transaction Documents:

(a) The Deed and Bill of Sale and the Assignment and Assumption are absolute, unconditional and indefeasible transfers of the property and interests in property described therein;

(b) The Undivided Interest is leased back by Owner Trustee to APS for an extendable term as provided in the Facility Lease, subject to the early termination and other provisions of the Facility Lease;

(c) APS's obligation to pay rent under the Facility Lease is absolute and unconditional as set forth in Section 4 of the Facility Lease; and

(d) The property and interests in property transferred by APS to Owner Trustee by the Deed and Bill of Sale and the Assignment and Assumption are to be owned by Owner Trustee upon expiration or earlier termination of the Facility Lease without further consideration passing from Owner Trustee to APS.

3. The Transaction Documents are an accurate and complete statement of the agreements, arrangements, and understandings of the parties thereto with respect to the transaction described in and contemplated by the Transaction Documents.

4. From the first contact of APS, Equity Participant and each other party to any Transaction Document and continuing through all discussions and negotiations among the parties to the Transaction Documents, the transaction described in and contemplated by the Transaction Documents has been intended and understood by APS, Equity Participant, and each other such party to be a sale and leaseback transaction.

IN WITNESS WHEREOF, APS has caused this Certificate to be executed on its behalf by its duly authorized officer as of August 18, 1986.

ARIZONA PUBLIC SERVICE COMPANY,
an Arizona corporation

By: _____

Its: Vice President

LAW OFFICES
SNELL & WILMER
3100 VALLEY BANK CENTER
PHOENIX, ARIZONA 85073
(602) 257-7211

August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Re: Arizona Public Service Company

Gentlemen:

We are members of the Arizona Bar and are general counsel to Arizona Public Service Company, an Arizona corporation (the "Company"). In that capacity, we are familiar with the matters relating to the preparation, execution and delivery of a Reimbursement Agreement (the "Reimbursement Agreement"), dated as of August 1, 1986, between the Company and Morgan Guaranty Trust Company of New York (the "Bank"). capitalized terms used herein and defined in the Reimbursement Agreement are used herein as therein defined.

In connection with the foregoing, we have examined, among other things, the following:

- (1) fully executed counterparts of the Reimbursement Agreement;
- (2) the fully executed Letter of Credit;
- (3) a recently certified copy of the Articles of Incorporation of the Company and all amendments thereto (the "Charter");
- (4) a recently certified copy of the Bylaws of the Company as now in effect (the "Bylaws");
- (5) a certificate of the Arizona Corporation Commission, dated August 11, 1986, attesting to the continued corporate existence and the good standing of the Company in that State; and certificates, telegrams, telexes (or have received telephone confirmations) from the State of New Mexico, dated as of a recent date, attesting to the qualification to do business and the good standing of the Company in that State; and

Morgan Guaranty Trust Company

New York

At 18, 1986

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(6) the Company's corporate proceedings and the proceedings before the Arizona Corporation Commission relating to the Reimbursement Agreement and related matters.

We have also examined the originals, or copies certified to our satisfaction, of the agreements, instruments and documents which affect or purport to affect the obligations of the Company under the Reimbursement Agreement and (i) such other corporate records of the Company, certificates of public officials and of officers of the Company, and (ii) such other agreements, instruments and documents, as we have deemed necessary as a basis for the opinions hereinafter expressed. As to questions of fact material to such opinions, we have, when relevant facts were not independently established by us, relied upon certificates of the Company or its officers or of public officials. We have assumed the due execution and delivery, pursuant to due authorization, of the Reimbursement Agreement by the Bank.

Based upon the foregoing and upon such other investigation as we have deemed necessary, we are of the opinion that, insofar as the laws of the State of Arizona are concerned:

(1) The execution, delivery and performance by the Company of the Reimbursement Agreement are within the Company's corporate power, have been duly authorized by all necessary corporate action, and do not contravene (i) the Charter or the Bylaws, or (ii) any law, rule or regulation or (iii) to the best of our knowledge, any contractual or legal restriction (including, but not limited to, the Existing Mortgage) binding on or affecting the Company, and do not result in or require the creation of any lien, security interest or other charge or encumbrance (other than pursuant to the Reimbursement Agreement) upon or with respect to any of its properties. The Reimbursement Agreement has been duly executed and delivered on behalf of the Company.

(2) The Arizona Corporation Commission has duly issued an order (Decision No. 55120) authorizing the Company to enter into the Reimbursement Agreement and to take all actions contemplated thereby or in connection therewith, and such order remains in full force and effect in the form issued. No other authorization, approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due

Morgan Guaranty Trust Company
New York
August 18, 1986
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execution, delivery and performance by the Company of the Reimbursement Agreement.

(3) The Reimbursement Agreement is the legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms; provided, however, that we express no opinion with respect to the enforceability of Sections 5 and 12 of the Reimbursement Agreement.

(4) There is no pending action or proceeding before any court, governmental agency or arbitrator against or directly involving the Company or any of its subsidiaries and, to the best of our knowledge, there is no pending or threatened action or proceeding affecting the Company or any of its subsidiaries before any court, governmental agency or arbitrator (A) in which any question is raised as to the validity of the Reimbursement Agreement, or (B) (except as set forth in (i) the Company's Report on Form 10-K for the fiscal year ended December 31, 1985 in Item 1 thereof under "Rates-State," "Environmental Requirements," "Generating Stations," "Water Supply" and "Indian Matters" or in Item 2 thereof, (ii) the Company's Report on Form 10-Q for the fiscal quarter ended March 31, 1986 under "Environmental Requirements," "Retail Rates," and "Palo Verde Nuclear Generating Station," and (iii) the Company's Report on Form 10-Q for the fiscal quarter ended June 30, 1986 under "Water Supply," "Retail Rates," and "Palo Verde Nuclear Generating Station") in which there is any material likelihood of an outcome which may materially and adversely affect the ability of the Company to perform its obligations under the Reimbursement Agreement. There has been no determination (interim or final) in any action or proceedings so disclosed which determination may materially adversely affect the ability of the Company to perform its obligations under the Reimbursement Agreement.

The opinions set forth above are subject to the following qualifications:

(a) The enforceability of the Company's obligations under the Reimbursement Agreement is subject to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors' rights generally.

(b) The enforceability of the Company's obligations under the Reimbursement Agreement may be subject to

Morgan Guaranty Trust Company
of New York
August 18, 1986
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general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

(c) We are not experts in the laws of the State of New York. In giving the opinion set forth in paragraph 4 above, we have relied, insofar as the laws of the State of New York are concerned, on the opinion of Mudge Rose Guthrie Alexander and Fardon delivered to you pursuant to Section 3(b)(11) of the Reimbursement Agreement.

We acknowledge that we are delivering to you, and you are entitled to rely upon, a separate opinion letter, dated the date hereof, concerning the enforceability of the Transaction Documents and related matters.

Very truly yours,

AIO262

LAW OFFICES
SNELL & WILMER
3100 VALLEY BANK CENTER
PHOENIX, ARIZONA 85073
(602) 257-7211

August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Re: Arizona Public Service Company:

Gentlemen:

We have acted as general counsel for Arizona Public Service Company, an Arizona corporation ("APS"), in connection with the transactions contemplated by the Participation Agreement, dated as of August 1, 1986 (the "Participation Agreement"), among the Equity Participant listed on the attached Schedule, Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants under the Bank Agency Agreement, The First National Bank of Boston, a national banking association ("FNB"), individually and as Owner Trustee, PVNGS Funding Corp., Inc., a Delaware corporation, Chemical Bank, a New York banking corporation, in its individual capacity and as Indenture Trustee, and APS. We are also familiar with the matters relating to the preparation, execution and delivery of a Reimbursement Agreement (the "Reimbursement Agreement"), dated as of August 1, 1986, between APS and Morgan Guaranty Trust Company (the "Bank"). All capitalized terms used herein and not otherwise defined herein shall have the meanings set forth in Appendix A to the Participation Agreement. This opinion is being delivered pursuant to Section 11(a)(20) of the Participation Agreement and Section 3(b)(i) of the Reimbursement Agreement.

As such counsel we have examined originals or copies, certified or otherwise identified to our satisfaction, of such corporate records, agreements and other instruments, certificates, orders, opinions, correspondence with public officials, certificates of officers and representatives of APS, and other documents, as we have deemed necessary or advisable for the purposes of rendering the opinions set forth herein.

In rendering our opinions, we have also reviewed the Special Order of Exemption, issued December 26, 1985, by

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the Arizona Department of Real Estate with respect to PVNGS, together with two (2) Snell & Wilmer petition letters to the Arizona Department of Real Estate, dated December 19, 1985 and December 23, 1985.

In rendering our opinions, we have relied as to certain factual matters on the documents we have examined, on certificates of public officials, and on the Certificate attached as Exhibit A, and we have assumed:

1. Each party to each Transaction Document, other than APS, is duly organized and validly existing in good standing under the laws of the jurisdiction of its organization, is duly registered, licensed or authorized to transact business in each other jurisdiction in which such registration, licensing or authorization is required, and has the power and the authority to enter into and to perform its obligations under each Transaction Document to which it is a party.

2. The execution, delivery and performance by each party to each Transaction Document, other than APS, have been duly authorized by all necessary action by such party and do not require the consent or approval of any of the stockholders of such party or, if required, such consent or approval has been obtained. Each Transaction Document has been duly executed and delivered by each party thereto, other than APS, and constitutes the legal, valid and binding obligation of such party, enforceable against such party in accordance with its terms.

3. The trusts of which the Owner Trustee and the Indenture Trustee are the Owner Trustee and the Indenture Trustee, respectively, were duly formed and are validly existing under the laws of the jurisdiction governing such trusts. Each of the Owner Trustee and the Indenture Trustee has the power and authority under the trust agreement for its respective trust to enter into and perform its obligations under each Transaction Document to which it is a party.

4. The Indenture Trustee is licensed, chartered, or regulated by the Federal Deposit Insurance Corporation or the Comptroller of the Currency.

5. The execution, delivery and performance by the Owner Trustee and the Indenture Trustee of each Transaction Document to which it is a party are authorized by the trust

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agreement of its respective trust and do not require the consent or approval of any other Person. Each Transaction Document to which the Owner Trustee or the Indenture Trustee is a party has been duly executed and delivered by the Owner Trustee or the Indenture Trustee, respectively, and constitutes the legal, valid and binding obligation of the Owner Trustee or the Indenture Trustee, respectively, enforceable against the Owner Trustee or the Indenture Trustee, respectively, in accordance with its terms.

6. Immediately prior to the execution and delivery of the Transaction Documents, APS owned the property to be transferred by APS to Owner Trustee under the Transaction Documents. Based on our knowledge, without independent investigation, we have no reason to believe this assumption is invalid. The assumption in this Paragraph 6 does not apply to the opinion in the first sentence of Section 14 of this legal opinion.

7. Amendment Number 10 to the ANPP Participation Agreement has been duly authorized, executed and delivered by APS, constitutes the legal, valid and binding agreement of, and is enforceable against, each of the parties thereto (other than APS).

8. The Transaction Documents accurately and completely set forth all agreements, arrangements and understandings of the parties thereto with respect to the transaction described in and contemplated by the Transaction Documents.

9. The Facility Lease is a "lease" and not a financing arrangement for Federal income tax purposes and an "operating lease" and not a "capital lease" for financial reporting purposes under Financial Accounting Standards Board Statement 13 and will be so treated and reported for such purposes by APS and Owner Trustee.

Based on the foregoing and subject to the qualifications set forth herein, it is our opinion as of the date hereof that:

1. APS is a corporation duly organized and validly existing in good standing under the laws of the State of Arizona and has the corporate power and authority to carry on its business as presently conducted, to own or hold under lease its properties and to enter into and perform its obli-

gations under the Participation Agreement, the Reimbursement Agreement and each other Transaction Document to which APS is a party. APS is duly qualified and in good standing to do business as a foreign corporation in the State of New Mexico and has not failed to qualify to do business or to be in good standing in any other jurisdiction where failure so to qualify or be in good standing would materially and adversely affect the financial condition or operations of APS or its ability to perform any obligations under the Participation Agreement, the Reimbursement Agreement or any other Transaction Document to which APS is a party.

2. The execution, delivery and performance by APS of the Participation Agreement and each other Transaction Document to which APS is a party have been duly authorized by all necessary corporate action on the part of APS and do not require the consent or approval of the stockholders of APS or any trustee or holder of any indebtedness or other obligation of APS, other than such consents and approvals as have been duly obtained, given or accomplished.

3. The Participation Agreement and each other Transaction Document to which APS is a party have been duly executed and delivered by APS and constitute the legal, valid and binding agreement of APS, enforceable against APS in accordance with their respective terms (other than the Facility Lease, which is discussed in Section 16 below). The opinions set forth in this Section 3 are subject to the qualifications that (i) enforceability of the Participation Agreement and the other Transaction Documents to which APS is a party in accordance with their respective terms may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting enforcement of creditors' or lessors' rights generally, as well as general principles of equity and the availability of equitable remedies, and (ii) certain laws and judicial decisions may affect the enforceability of certain rights and remedies provided in the Transaction Documents. With respect to the latter qualification, however, we are of the opinion that none of such laws now in effect and none of such judicial decisions presently existing make the rights and remedies provided in the Transaction Documents, taken as a whole, inadequate for the realization of the benefits of the Transaction Documents.

4. Neither the execution, delivery or performance by APS of its obligations pursuant to the Participation Agreement or any other Transaction Document to which APS is a

party, nor the consummation by APS of the transactions contemplated thereby, nor compliance by APS with the provisions thereof, conflicts with, or results in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or Bylaws of APS or, to the best of our knowledge after due inquiry, any Affiliate of APS, or, to the best of our knowledge after due inquiry, any indenture, mortgage, lease or any other agreement or instrument to which APS or any Affiliate of APS is a party or by which the property of APS or any Affiliate of APS is bound, or results in the creation or imposition of any Lien (other than Permitted Liens) upon any property of APS or any Affiliate of APS.

5. All Arizona Governmental Action which is required in connection with the execution, delivery or, as of the date hereof, performance by APS of its obligations pursuant to, or the consummation by APS of the transactions contemplated by, the Participation Agreement and any other Transaction Document to which APS is a party, have been duly obtained, given or accomplished, except that our opinion in this Section 5 does not relate to the recording or filing of any Transaction Documents, although we hereby confirm that we have submitted for recordation or filing the documents specified in Schedule 5 to the Participation Agreement (except those documents specified in Part IIC to such Schedule).

6. APS holds such valid franchises, certificates of convenience and necessity, licenses, and permits as are necessary with respect to the maintenance and operation of its property and business as now conducted, except that (a) APS from time to time makes minor extensions of its system prior to the time a related franchise, certificate, license, or permit is procured, (b) from time to time communities already being serviced by APS become incorporated and considerable time may elapse before a franchise is procured, (c) certain franchises may have expired prior to the renegotiation thereof, (d) APS may not have obtained certain permits or variances relating to the environmental requirements described under "Environmental Requirements" in Item 1 in APS's Report on Form 10-K for the fiscal year ended December 31, 1985, and (e) certain minor defects and exceptions may exist which, individually and in the aggregate, are not deemed material.

7. Except as disclosed in the financial statements to which reference is made in Section 10(a)(11) of the Participation Agreement and in the reports to which reference

August 18, 1986

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is made in Section 10(a)(12) of the Participation Agreement, there is no action, suit, investigation or proceeding pending or, to our knowledge after due inquiry, threatened against APS before any federal or Arizona court, arbitrator or administrative or governmental body which questions the validity or enforceability of the Participation Agreement, any other Transaction Document in effect on the date hereof, or the ANPP Participation Agreement, or which, individually or in the aggregate, if decided adversely to the interests of APS, would have a material adverse effect on the business or financial condition of APS or materially and adversely affect the ability of APS to perform its obligations under the Participation Agreement or any other Transaction Document in effect on the date hereof to which APS is a party.

8. The lien of the Existing Mortgage does not extend to contract rights of APS under the Transaction Documents (other than the Facility Lease) or to the Generation Entitlement Share related to the Undivided Interest.

9. Under Arizona Applicable Law, neither the Loan Participants, Funding Corporation, the Equity Participant, Bank nor FNB (in its individual capacity and as Owner Trustee) will be or become, solely by reason of the activities contemplated by the Transaction Documents or the Reimbursement Agreement prior to the expiration or termination of the Facility Lease, subject to regulation as a public service corporation, public utility, or a public utility holding company by any Arizona public utility commission or other Arizona regulatory body, authority or group (including, without limitation, the Arizona Corporation Commission), provided, however, that we express no opinion regarding the effect of (i) any transfer of ownership of the Undivided Interest or the Real Property Interest by the Owner Trustee, (ii) termination or expiration of the Facility Lease and the taking of possession by the Owner Trustee or any other Person of an interest in Unit 2, (iii) APS's providing of transmission services for the Owner Trustee or any other Person owning the Undivided Interest or the Real Property Interest, or (iv) any exercise of remedies or other rights by any Person in connection with taking possession of an interest in Unit 2.

10. APS is a "subsidiary company" of a "holding company," AZP Group, Inc., and an "affiliate" of a "holding company," as such terms are defined in the Holding Company Agreement, but APS is exempt from all provisions of the Holding

Company Act and the rules thereunder (except Section 9(a)(2) of the Holding Company Act).

11. The execution, delivery and performance of the Transaction Documents or the Reimbursement Agreement by the parties thereto do not violate the Atomic Energy Act, as now in effect, the NRC regulations now in effect, or any order of the NRC now in effect, provided that such parties comply with the terms and conditions of the License. No Governmental Action by or with respect to the NRC is or will be required in connection with the execution, delivery or performance by APS of the Participation Agreement, the Reimbursement Agreement, the Facility Lease, the Assignment and Assumption or any other Transaction Document to which it is a party, except (i) such Governmental Actions as may be required pursuant to the express terms of the License; (ii) such other Governmental Actions by or with respect to the NRC as have been duly obtained, given or accomplished on or before the date hereof; (iii) such Governmental Actions of or with respect to the NRC as it may determine after the Closing Date under existing law to be necessary to protect the public health and safety in connection with the construction, improvement, maintenance, operation, decommissioning or retirement from service by the Licensees described in the License of any portion of Unit 2 or PVNGS or otherwise with respect to Unit 2 or PVNGS; and (iv) such other Governmental Actions as may be required under Applicable Law not now in effect. The exercise by the Lessor and the Equity Participant of their respective rights and remedies under the Facility Lease and the other Transaction Documents, under the circumstances and for the purposes therein set forth, will not violate the License or the terms and conditions of such License, except to the extent that the NRC shall determine that the exercise of such rights and remedies will or may adversely affect the public health and safety.

12. The transfer of property and interests in Property by APS to the Owner Trustee pursuant to the Participation Agreement, the Bill of Sale, the Deed, and the Assignment and Assumption is not a fraudulent conveyance under the law of the State of Arizona, provided, however, that this opinion, in so far as it relates to A.R.S. Section 44-1061 and any common law vendor-in-possession fraudulent conveyance doctrine, is subject to the following comments. A.R.S. Section 44-1061 provides:

"A. A sale made by a vendor of goods and chattels in his possession or under his

Morgan Guaranty Trust Company
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control, or an assignment of goods and chattels, unless the sale or assignment is accompanied by an immediate delivery and followed by an actual and continued change of possession of the things sold or assigned, is prima facie evidence of fraud against creditors of the vendor, or creditors of the person making the assignment, or subsequent purchasers in good faith.

"B. The term 'creditors' includes all persons who are creditors of the vendor or assignor at any time while such goods and chattels are in his possession or under his control."

The Arizona court decisions interpreting A.R.S. Section 44-1061 arose in the context of tangible property in the actual possession of the seller. These decisions suggest that open, visible and unequivocal indications that there has been change of ownership would be sufficient to overcome the prima facie evidence of fraud established by Section 44-1061. See, e.g., *Nolte v. Winstanley*, 16 Ariz. 327, 145 P. 246 (1914). Unfortunately, this precedent is not very helpful in the context of the present transaction. In addition, the court decisions under A.R.S. Section 44-1061 are equivocal as to the effect of recording or filing transfer documents. *Nolte v. Winstanley*, *supra*; and *Leibes v. Steffy*, 4 Ariz. 11, 32 P. 261 (1893). Notwithstanding this equivocation, as to a subsequent encumbrancer of any personal property which is subject to Article 9 of the Uniform Commercial Code as in effect in Arizona, which is described in the three (3) UCC-1 Financing Statements, dated August 18, 1986 between APS, as the lessee, and Owner Trustee, as lessor, filed with the Secretary of State of Arizona and the County Recorder, Maricopa County, State of Arizona (the "Lease Financing Statements") and in which a security interest may be perfected by filing of a financing statement within Arizona, we believe that the filing of the Lease Financing Statements should be sufficient to overcome the prima facie evidence of fraud to the extent the description of such property in the Lease Financing Statements is accurate and complete. In addition, as to future creditors with actual knowledge of the transfers in the Deed, the Bill of Sale, and the Assignment and Assumption prior to extending or committing to extend credit, we believe that such knowledge should overcome the prima facie evidence of fraud in A.R.S. Section 44-1061.

13. Neither the execution and delivery by APS of, nor the performance by APS of its obligations under, any Transaction Document to which it is a party, conflicts with, or results in a breach of any statute, ordinance, governmental rule or regulation of the State of Arizona or Maricopa County, except that our opinion in this Section 13 does not relate to any conflict or breach after the date hereof as a result of (i) the construction, improvement, maintenance, use, possession, operation, decommissioning or retirement from service of any portion of Unit 2 or PVNGS or otherwise with respect to Unit 2 or PVNGS or APS's or the Operating Agent's involvement therewith, APS's duties and obligations as an ANPP Participant under any of the ANPP Project Agreements, or APS's duties and obligations as Agent under the Assignment and Assumption; (ii) securities and taxation laws of any Arizona Governmental Authority; (iii) any Releveraging, Refunding, or Reoptimization described in Sections 2(d), 2(e) and 2(f) of the Participation Agreement; (iv) any Supplemental Financing pursuant to Section 8(f) of the Facility Lease; (v) any action taken by APS pursuant to Section 10(b)(2) of the Participation Agreement or any similar provision in the Participation Agreement or any other Transaction Document; (vi) any involvement by APS in connection with any transfer of ownership of the Undivided Interest or the Real Property Interest by the Owner Trustee or the taking of possession of the Undivided Interest or the Real Property Interest by Owner Trustee or any other Person upon expiration or termination of the Facility Lease or otherwise; (vii) APS providing transmission services for the Owner Trustee or any other Person owning the Undivided Interest or the Real Property Interest or ceasing to serve as Agent pursuant to the Assignment or Assumption; (viii) any action by APS pursuant to Article VII of the Assignment and Assumption; (ix) Lessor or any other Person, other than APS, receiving the Generation Entitlement Share of APS, pursuant to Section 19 of the Facility Lease or any other provision of any Transaction Document; or (x) any payment by APS pursuant to Sections 14(b) or 16 of the Participation Agreement or any similar provision in the Participation Agreement or any other Transaction Document.

14. Assuming that any choice of law provision in favor of the law of a state other than the State of Arizona is disregarded therein, (i) the Deed, the Bill of Sale and the Assignment and Assumption are in sufficient form to convey from APS to Owner Trustee the interests in property described therein and for recording under the law of the State

of Arizona and (ii) the Indenture is in sufficient form to grant from Owner Trustee to Indenture Trustee the security interest and mortgage described therein and for recording under the law of the State of Arizona. The Deed, the Bill of Sale, the Assignment and Assumption, the Facility Lease and the Indenture when duly executed, acknowledged and delivered, must each be recorded in the Office of the Recorder of Maricopa County, Arizona, together with an Affidavit of Legal Value pursuant to A.R.S. Section 42-1612 with respect to any such document transferring title to real estate (other than leases or easements). Precautionary financing statements pursuant to A.R.S. Section 47-9408 and financing statements naming the Owner Trustee, as debtor, and the Indenture Trustee, as secured party, in respect of the Lease Indenture Estate must be filed in the office of the Arizona Secretary of State and recorded in the Office of the Recorder of Maricopa County, Arizona. We hereby confirm that we have submitted for recordation or filing the documents referred to in the two (2) preceding sentences. Upon the completion of such recordings and filings and except as explained below, no other filings or recordings in Arizona are required to establish, preserve, perfect, and protect (i) the Owner Trustee's rights and interests (including, without limitation, any security interest which may be deemed to be created by the Facility Lease) in and to the Undivided Interest and the Real Property Interest and (ii) the security interest of the Indenture Trustee in the Lease Indenture Estate, and no additional recordation is required to continue the effectiveness of such recordings, provided that our opinion in this Section 14 is limited to property constituting the Undivided Interest, the Real Property Interest and the Lease Indenture Estate that is either real property under the law of the State of Arizona or property subject to Article 9 of the Uniform Commercial Code (as in effect in Arizona) in which a security interest may be perfected by the filing of a financing statement within the State of Arizona. In addition, no additional financing statements, other than those filed with the Secretary of State of Arizona and recorded in the Office of the County Recorder of Maricopa County, Arizona, are required to be filed in order to continue the effectiveness thereof except that continuation statements are required to be filed with respect to such financing statements within each of the six-month periods preceding the expiration of each six-year period after the respective dates of filing. We express no opinion regarding the form for conveyance, the transfer or the perfection of rights in any Capital Improvements or regarding filings or recordings that may be required

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under the laws of any other state, under federal law or by reason of the application of the conflict of laws rules set forth in A.R.S. Section 47-9103. To the extent any recorded or filed Transaction Document refers to or incorporates by reference any other document (for definitional purposes or otherwise) not recorded or filed in the same location or if recorded or filed, not identifying the date and instrument or file number of such document incorporated by reference, our opinion in this Section 14 excludes the effect, if any, of such reference or incorporation by reference. In giving our opinion in this Section 14 we have assumed that the description of the Undivided Interest, the Real Property Interest and the Lease Indenture Estate in the Transaction Documents is accurate and complete.

15. You have requested that we advise you whether an Arizona court would give effect to the choice of law provision in favor of the law of the State of New York in each Transaction Document, other than the Deed, the Bill of Sale, the Assignment and Assumption, and the Facility Lease. There is no Arizona case stating that an Arizona court will follow the choice of law provision of the parties to a contract. However, the Supreme Court of Arizona has consistently ruled that where it is not bound by a previous decision or by legislative enactment it will follow the rules in the *Restatements of the Law* including the *Restatements of Conflict of Laws*. *Smith v. Normat*, 51 Ariz. 134, 75 P.2d 38 (1938); *Western Coal & Min. Co. v. Hilvert*, 63 Ariz. 171, 160 P.2d 331 (1945); and *Taylor v. Security National Bank*, 20 Ariz. App. 504, 514 P.2d 257 (1973). Section 187 of the *Restatement (Second) of Conflict of Laws* provides that the parties to a contract may stipulate to their choice of law to govern the contract and that the laws of the state chosen will be applied unless (i) the particular issue is one which the parties could not have resolved by an explicit provision in their agreement directed to that issue, and (ii) either:

"(a) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or

"(b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the

"chosen state in the determination of the particular issue and which, under the rule of Section 188, would be the state of the applicable law in the absence of an effective choice of law by the parties."

We believe that the State of New York has a "substantial relationship" to the parties or the transaction with respect to the documents covered by the opinion in this Section 15 and that with respect to such documents there is a reasonable basis for the choice of law of the State of New York because at least one of the parties to such documents is located in the State of New York and such documents have been substantially negotiated within and from the State of New York and have been executed and delivered within the State of New York. Thus, the effectiveness of the choice of law provisions in these documents will depend upon whether, as to the particular issue in question, (i) there would be a difference in the applicable substantive law of the State of New York, on the one hand, and the law of the State of Arizona or another state, on the other hand, (ii) the resolution of such issue under the law of the State of New York would be contrary to a fundamental policy of the State of Arizona or such other state, (iii) the State of Arizona or such other state would have a materially greater interest than the State of New York in the determination of the particular issue and (iv) under Section 188 of the *Restatement (Second) Conflict of Laws*, the law of the State of Arizona or such other state would be the applicable law.

16. Assuming an Arizona court were not to give effect to the choice of law provision in the Facility Lease in favor of the law of the State of New York and were to apply the law of the State of Arizona (other than choice of law rules), the Facility Lease is the legal, valid, and binding obligation of APS and is duly enforceable against APS in accordance with its terms:

(a) Except as limited by applicable bankruptcy, insolvency, moratorium, reorganization, and similar laws of general application;

(b) Except as limited by equitable principles of general application; and

(c) Except as limited by other applicable laws or general principles of law that may render unenforceable

certain provisions of the Facility Lease, provided, however, that (i) if Owner Trustee does not violate the terms of the License referenced in Section 11 of this legal opinion and Owner Trustee fulfills the duty, if applicable, to mitigate losses, such limitations will not interfere with the enforcement by Owner Trustee of the obligations of APS to pay Basic Rent as provided in Section 3(a) of the Facility Lease as the payments of Basic Rent become due on each Basic Rent Payment Date prior to termination of the Facility Lease and without acceleration or advancement thereof and (ii) Owner Trustee may obtain the return of the Undivided Interest and the Real Property Interest upon termination or expiration of the Facility Lease, except in the case of each of (i) and (ii) for the economic consequences of any procedural delays that may result from such limitations.

Anything in this opinion to the contrary notwithstanding, we express no opinion concerning (i) the ownership of, or legal or equitable title to, any property, (ii) whether the property described and referred to in the Transaction Documents is personal property or real property or whether any severance or other provision in the Transaction Documents purporting to make certain property personal property is effective, or (iii) the priority of the interest of any person in any property or interest in property.

In rendering the opinions set forth above, we have relied as to all matters relating to the law of the State of New York, solely upon the opinion of Mudge Rose Guthrie Alexander & Ferdon, Special Counsel for APS, delivered pursuant to Section 11(a)(19) of the Participation Agreement, as to which law we have, with your consent, made no independent investigation. Subject to the foregoing qualification, the above opinions are limited to the laws of the State of Arizona as in effect on the date of this opinion and we express no opinion as to the applicability or effect of federal law, except as set forth in Sections 10 and 11 of this opinion and as federal law is in effect on the date of this opinion, or the law of any state other than Arizona. This opinion is rendered to you solely in connection with the transactions described in and contemplated by the Transaction Documents. This opinion is not to be referred to, or quoted in, any document, report, or financial statement or filed with, or delivered to, any governmental entity or other person or entity, without our prior written consent.

Very truly yours,

FC888

August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

SALE AND LEASEBACK OF AN UNDIVIDED INTEREST IN
PALO VERDE NUCLEAR GENERATING STATION UNIT 2

Dear Sirs:

We have acted as special New York counsel for Arizona Public Service Company, an Arizona corporation (APS), in connection with the transactions contemplated by (i) the Participation Agreement, dated as of August 1, 1986 (the Participation Agreement), among Emerson Finance Co., a Delaware corporation, as Equity Participant, PVNGS Funding Corp., Inc., a Delaware corporation (Funding Corp), Bank of America National Trust and Savings Association, for itself and as Agent for the Original Loan Participants listed on Schedule 1 to the Participation Agreement, The First National Bank of Boston, a national banking association, individually and as Owner Trustee, Chemical Bank, a New York banking corporation, individually and as Indenture Trustee, and APS and (ii) the Reimbursement Agreement, dated as of August 1, 1986 (the Reimbursement Agreement), between APS and Morgan Guaranty Trust Company of New York, a New York trust company (the Bank). All capitalized terms used herein and not otherwise defined herein or in Section 1 to the Reimbursement Agreement shall have the meanings assigned thereto in Appendix A to the Participation Agreement. This opinion is being delivered pursuant to Section 3(b)(ii) of the Reimbursement Agreement.

As such counsel we have examined originals or copies, certified or otherwise identified to our satisfaction, of such corporate records, agreements and other instruments, certificates, opinions, correspondence with public officials, certificates of officers,

management personnel and representatives of APS, and such other documents, as we have deemed necessary or advisable for the purposes of rendering the opinions set forth herein.

Based on the foregoing and subject to the qualifications set forth below, we are of the opinion that:

(1) The Reimbursement Agreement and each Transaction Document to which APS is a party have been duly executed and delivered by APS, and, assuming the due authorization, execution and delivery thereof by the other parties thereto (other than Funding Corp), the Reimbursement Agreement and each Transaction Document to which APS is a party constitute the legal, valid and binding agreements of APS, enforceable against APS in accordance with their respective terms.

(2) Neither the execution, delivery or performance by APS of the Reimbursement Agreement or any Transaction Document to which APS is a party, nor the consummation by APS of the transactions contemplated thereby, nor compliance by APS with the provisions thereof, conflicts with, or results in a breach or contravention of any of the provisions of, the Restated Articles of Incorporation or By-Laws of APS, or any Federal or New York Applicable Law.

(3) No Governmental Action under any Federal or New York law now in effect is required in connection with the execution, delivery or performance by APS of, or the consummation by APS of the transactions contemplated by, the Reimbursement Agreement or any Transaction Document to which APS is a party, except such Federal and New York Governmental Actions (i) as have been duly obtained, given or accomplished, (ii) as are routine in nature and that cannot be obtained, or are not normally applied for, prior to the time they are required, (iii) as may be required to be obtained, given or accomplished from time to time in connection with the maintenance, use, possession, operation or improvement of Unit 2 or otherwise with respect to Unit 2 and APS's or the Operating Agent's involvement therewith, (iv) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (v) as may be required in consequence of the issuance, sale or exchange and delivery of or any obligations issued under and pursuant to any Collateral Trust Indenture, (vi) as may be required by existing Applicable Law on and after termination or expiration of the Facility Lease, or (vii) as may be required under Federal or New York law not now in effect. No Federal or New York Governmental Action is or will be required (a) solely

by virtue of the participation by the Bank or any Participant in the consummation of the transactions contemplated by the Reimbursement Agreement to take place on the date hereof or by the Owner Trustee, the Indenture Trustee, the Equity Participant, Funding Corp or any Loan Participant in the consummation of the transactions contemplated by the Transaction Documents to take place on the date hereof or (b) to be obtained by any of such Persons during the term of the Facility Lease with respect to Unit 2 except, in each case, such Federal or New York Governmental Actions (i) as have been duly obtained, given or accomplished, (ii) as may be required by Applicable Law not now in effect, (iii) as may be required in consequence of any transfer of ownership of any Note or Bond by the Holder thereof, the beneficial interest in the Trust by the Equity Participant, or the Undivided Interest or the Real Property Interest by the Owner Trustee, (iv) as may be required in consequence of the issuance, sale or exchange and delivery of or any obligations issued under and pursuant to any Collateral Trust Indenture, (v) as would be required by Applicable Law existing on the Lease Termination Date in connection with taking possession of an interest in Unit 2, (vi) as may be required under the Holding Company Act in the event that no proper filing by the Owner Trustee and the Equity Participant of Form U-7D with the SEC is made on or within 30 days after the date hereof, or (vii) as may be required in consequence of any exercise of remedies or other rights by any such Person under Section 16 of the Facility Lease or otherwise in connection with taking possession of an interest in Unit 2.

(4) So long as the Facility Lease is in effect, assuming the proper filing by the Owner Trustee and the Equity Participant of Form U-7D with the SEC on or within 30 days after the date hereof, under Federal law now in effect, neither the Bank, any Loan Participant, the Equity Participant, FNB nor the Owner Trustee will be or become, solely by reason of either its entering into the Reimbursement Agreement or any Transaction Document to which any of them is a party, or the transactions contemplated thereby, subject to regulation as an electric utility company, an electric utility, a public-utility company or corporation, a public utility, a holding company, a public utility holding company, an electric corporation, or a utility company or corporation by any Federal or New York public utility commission or other regulatory body, authority or group (including, without limitation, the SEC and the FERC).

(5) APS is not an "investment company", or a company "controlled" by an "investment company", within the meaning of the Investment Company Act.

The opinions set forth above are subject to the qualifications that (i) enforceability of the Reimbursement Agreement and the Transaction Documents to which APS is a party in accordance with their respective terms may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting enforcement of creditors' or lessors' rights generally, as well as general principles of equity, and (ii) certain laws and judicial decisions may affect the enforceability against APS of certain rights and remedies provided in the Transaction Documents. With respect to the latter qualification, however, we are of the opinion that none of such laws now in effect and none of such judicial decisions make the rights and remedies provided in the Transaction Documents, taken as a whole, inadequate for the realization of the benefits of the Transaction Documents.

This opinion is limited to the laws of the State of New York and the Federal laws of the United States of America; however we express no opinion as to any matters relating to the Atomic Energy Act or the Nuclear Waste Act.

Very truly yours,

POLK & WARDWELL

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August 18, 1986

Morgan Guaranty Trust Company
of New York
23 Wall Street
New York, New York 10015

Dear Sirs:

We have acted as your counsel in connection with the preparation, execution and delivery of the Reimbursement Agreement dated as of August 1, 1986 (the "Reimbursement Agreement") between Arizona Public Service Company, an Arizona corporation (the "Company"), and Morgan Guaranty Trust Company of New York (the "Bank"). Terms defined in the Reimbursement Agreement are used herein as therein defined.

We have examined originals or copies, certified or otherwise identified to our satisfaction, of such documents, corporate records, certificates of public officials and other instruments and have conducted such other investigations of fact and law as we have deemed necessary or advisable for purposes of this opinion.

Upon the basis of the foregoing, we are of the opinion that the Reimbursement Agreement constitutes a valid and binding agreement of the Company enforceable in accordance with its terms except as (i) the enforceability thereof may be limited by bankruptcy, insolvency or similar laws affecting creditors' rights generally and (ii) rights of acceleration and the availability of equitable remedies

may be limited by equitable principles of general applicability.

In rendering the foregoing opinion, we have relied, without independent investigation, as to all matters of Arizona law upon the opinion, dated the date hereof, of Snell & Wilmer, counsel for the Company, delivered to you pursuant to Section 3(b)(i) of the Reimbursement Agreement, and our opinion is subject to the qualifications and exceptions therein expressed.

Very truly yours,

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On February 13, 1986, the date Unit 1 of the Palo Verde Nuclear Generating Station attained commercial operation as defined by the Arizona Corporation Commission (the "ACC"), the Company ceased accruing allowance for funds used during construction ("AFC") with respect to Unit 1 and the facilities common to all three Palo Verde Units (the "Common Facilities") in the amount of approximately \$6 million per month. In addition, the Company began expensing the cost of owning, operating and maintaining its 29.1% share of Unit 1 and the Common Facilities, currently totalling approximately \$5 million per month. Absent adequate and timely rate relief from the ACC, the Company expects these developments to continue to adversely affect its earnings.

On July 24, 1986, ACC issued an order concerning the purchased power and fuel adjustment mechanism ("PPFAM") of the Company in the "Phase I" hearing of the rate case in which the Company requested an increase in annual retail rates premised on Unit 1 of Palo Verde being fully included in the Company's rate base. To permit the Company to recover these fuel costs that the ACC found reasonable, the order authorized the Company to increase its "base fuel" charge to \$.016033 per kilowatt hour and established the PPFAM charge at \$.003099 per kilowatt hour (the "PPFAM Charge"), both of which became effective August 1, 1986. At June 30, 1986, the Company had under-collected fuel and purchased power costs of approximately \$66.2 million. Through the operation of the PPFAM Charge, the Company will recover approximately \$41.8 million of this amount over a period of approximately one year. The ACC disallowed recovery of the remainder of under-collected fuel and purchased power costs, approximately \$24.4 million, due to the Company's temporary sale of generating output from Unit 4 of the Cholla Plant to another utility. The Company, on August 11, 1986, filed a motion seeking reconsideration and rehearing of the ACC's order. A temporary PPFAM charge of \$.004 per kilowatt hour, designed to reduce the Company's under-collected fuel and purchased power costs, had been in effect since September 1985, pending the "Phase I" determination.