AVISTA Corp.

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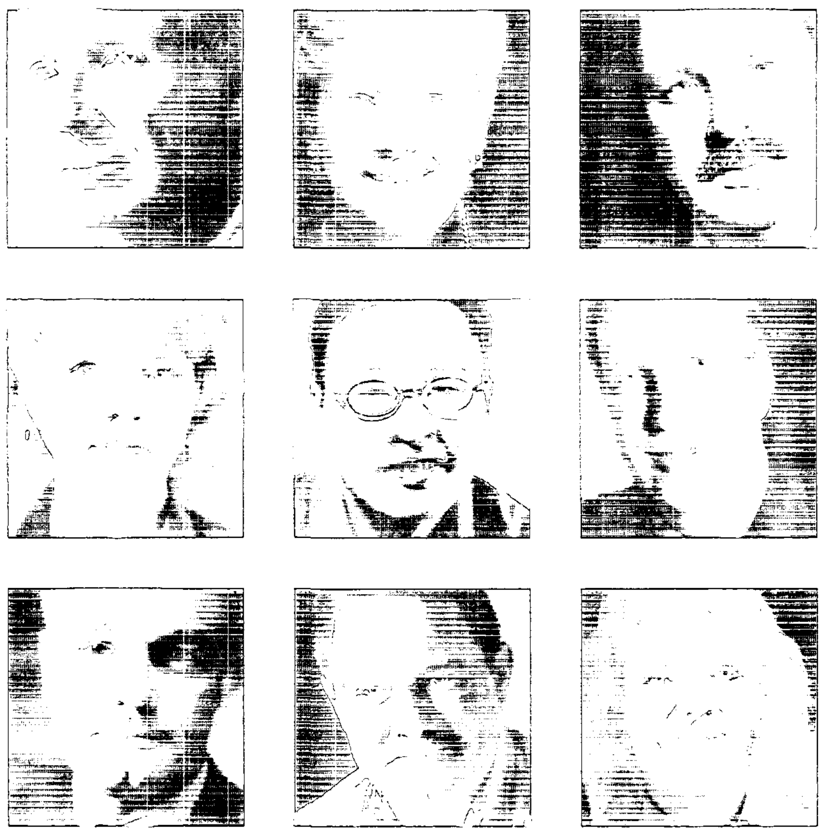

2002 SUMMARY ANNUAL REPORT

Ours is a practical company. If there's a straight line from an opportunity to an outcome that's good for business — and consistent with our values — we go forward.

Avista. We favor a direct approach.

AVISTA BUSINESSES

We are among the nation's most efficient and cost-competitive energy providers, with utility operations in five Western states. By focusing on our core utility business, Avista gains expertise directly applicable to our energy-related subsidiaries.

Regulated Business

Avista Utilities provides energy to 320,000 electric and 290,000 natural gas customers, primarily in the Pacific Northwest.

Unregulated Business

Avista Energy applies our energy marketing knowledge and experience to physical assets in Western regional markets.

Avista Advantage streamlines utility billing and related business processes for multi-site organizations.

Avista Labs develops clean, reliable modular fuel cell technology for distributed power markets.

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The right direction

Despite a fair degree of adversity, Avista gained strength and momentum in 2002.

Our two principal energy businesses operated profitably, providing the means to repurchase $204 million in high-cost debt. As a result, we achieved a debt ratio of 54 percent, reduced future interest expense and earned an upgrade in our credit outlook from Standard & Poor's. We further stabilized our financial footing with a Washington rate case agreement that includes a mechanism for more predictable future earnings. And we are well on our way to favorably resolving the Federal Energy Regulatory Commission's investigation into our energy trading practices, with no finding of improper activities.

The progress we've made is all the more striking in light of some truly serious obstacles. Like many in our industry, we confronted grave financial hardship in 2002. Adding to the strain were delays in a significant generation project and a political threat to our largest hydroelectric asset.

Such difficulties have repercussions, and Avista's 2002 results reflect that. Net income totaled $31 million on revenues of $980 million and earnings per diluted share of $0.60. Overall, our stock finished the year down 12.82 percent. This compares well to the Dow Jones industrial and utility averages, however, which were down 16.76 percent and 26.79 percent, respectively.

While it was a tough year, I remain upbeat — and with good reason. Any company as long-established as Avista finds a way to manage the ups and downs of business. We do so by holding fast to our guiding principles. No matter the situation or opportunity, these principles of trust, integrity, innovation, relationships and collaboration apply. And they steer us toward an outcome consistent with our values.

Our adherence to guiding principles accounts for the successes we realized in the midst of 2002's challenges. We drew on Avista's collaborative relationship with regulators in crafting an all-party settlement of the remaining issues in our general rate case before the Washington Utilities and Transportation Commission. Consequently, we will recover the vast majority of 2001's deferred power costs. We also were granted an energy recovery mechanism in Washington that, along with the regulatory tracking mechanisms in place for electric and natural gas operations in all the states we serve, will promote ongoing financial stability.

CONTINUED

Gary G. Ely has been with Avista for 36 of its 50 years on the New York Stock Exchange. It was an honor for Gary to preside over The Closing Bell™ on October 2, 2002. Several other long-time Avista employees joined him in this celebration of our golden anniversary as an NYSE-listed company.

Fewer than 10 percent of companies on the exchange reach that landmark. We're pleased to be among them.

In order to maintain a good relationship with you, our shareholders, we've undertaken additional measures to restore value. Avista Energy's continued success, along with Avista Utilities' improved performance, provided much of the cash we used to reduce total outstanding debt by $248 million by year-end. We intend, through similar strategies, to persevere in elevating our financial performance and, over time, to regain our investment-grade credit rating.

Our customers' trust is equally important to us, and the past year saw us reach our goal of owning or controlling sufficient generation to meet their needs. We overcame some serious impediments to achieve the level of reliability we're determined to provide current and future customers — including a number of unavoidable delays in completing our Coyote Springs 2 plant and a Montana voter initiative that attempted to transfer title of the state's privately owned hydroelectric projects to the public. The measure was defeated, preserving our long-time ownership of Noxon Rapids Dam.

All that progress aside, we understand, of course, that you are less interested in what we have done than in what we will do. Here is what you can expect from Avista in the months and years ahead: continued reduction of our debt ratio and interest costs, in part through earnings contributions from Avista Energy; improved Avista Utilities earnings through cost controls and price increases, where appropriate; and renewed focus on revenue growth at the utility through such measures as increased commercial and industrial sales, and economic development programs.

In addition, we'll remain disciplined in our approach to Avista Labs and Avista Advantage. Both these businesses met key milestones in 2002. And although market conditions have hampered our efforts to find a partner for Avista Labs, we are in discussions with several parties. Our goal is less than 20 percent ownership of this subsidiary. At Avista Advantage, we'll continue our push toward sustained profitability.

There's a long road ahead for Avista. It may take another two years for us to reach the solid financial position you — and I — expect of us. We do have several things working in our favor, including a resource base that provides our customers some of the lowest-cost electricity in the nation. And we have the finest, most capable people I know working on the task. You'll read about a few of them in the pages that follow. Most Avista employees are shareholders just like you, and they have your best interests in mind. You can count on that.

Gary G. Ely
Chairman, President and
Chief Executive Officer

March 14, 2003

FINANCIAL AND OPERATING HIGHLIGHTS

(Dollars in Thousands Except Statistics and Per Share Amounts or as Otherwise Indicated)	2002	2001	2000
Financial Results			
Operating revenues	$ 980,446	$1,395,313	$ 1,858,516
Operating expenses	835,759	1,226,021	1,641,428
Income from operations	144,687	169,292	217,088
Income from continuing operations	34,310	59,605	101,055
Income (loss) from discontinued operations	1,145	(47,449)	(9,376)
Net income before cumulative effect of accounting change	35,455	12,156	91,679
Cumulative effect of accounting change	(4,148)	—	—
Net income	31,307	12,156	91,679
Income available for common stock	28,905	9,724	67,944
Earnings per common share from continuing operations, diluted	0.67	1.20	1.67
Earnings (loss) per common share from discontinued operations, diluted	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change, diluted	0.69	0.20	1.47
Loss per common share from cumulative effect of accounting change, diluted	(0.09)	—	—
Earnings per common share, diluted	0.60	0.20	1.47
Earnings per common share, basic	0.60	0.21	1.49
Dividends paid per common share	0.48	0.48	0.48
Book value per common share	14.84	15.12	15.34
Average common shares outstanding	47,823	47,417	45,690
Actual common shares outstanding	48,044	47,633	47,209
Return on average common equity	4.0%	1.3%	12.9%
Common stock closing price	11.56	13.26	20.50
Operating Results			
AVISTA UTILITIES			
Retail electric revenues	$ 463,667	$ 398,441	$ 394,439
Retail kWh sales (in millions)	7,584	8,018	8,238
Retail electric customers at year-end	320,210	316,694	313,290
Wholesale electric revenues	$ 64,082	$ 480,903	$ 864,754
Wholesale kWh sales (in millions)	2,216	6,262	15,807
Total natural gas revenues	$ 309,823	$ 308,643	$ 224,846
Total therm sales (in thousands)	516,491	541,984	595,902
Total natural gas customers at year-end	290,278	284,420	278,982
Net income (loss)	$ 36,382	$ 24,164	$ (38,781)
ENERGY TRADING AND MARKETING			
Revenues	$ 54,207	$ 134,266	$ 307,746
Net income	22,425	63,246	161,753
kWh sales (in millions)	40,426	47,927	105,548
Natural gas sales (thousands of dekatherms)	225,983	248,193	273,448
Coal sales (thousands of tons)	—	—	3,514
INFORMATION AND TECHNOLOGY			
Revenues	$ 17,630	$ 13,815	$ 5,732
Net loss	(12,117)	(19,384)	(19,032)
OTHER			
Revenues	$ 14,645	$ 16,385	$ 32,937
Net loss	(12,380)	(8,421)	(2,885)
Other Financial and Operating Statistics			
Total assets	$3,614,133	$4,037,223	$12,577,081
Total net utility property	1,563,704	1,565,642	1,518,312
Utility capital expenditures	64,207	119,905	98,680
Total capitalization:			
Long-term debt	902,635	1,175,715	679,806
Preferred trust securities	100,000	100,000	100,000
Preferred stock	33,250	35,000	35,000
Common equity	712,791	720,063	724,224
Total Capitalization	$1,748,676	$2,030,778	$ 1,539,030

2002 MILESTONES

Avista advanced on several fronts over the course of the year.

FINANCIAL

- We strengthened our financial position with improved operating cash flow and earnings.

- Standard & Poor's upgraded its credit outlook to stable and affirmed its credit ratings for Avista.

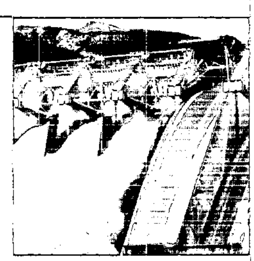
Malyn K. Malquist

- Malyn K. Malquist joined the company as our chief financial officer and senior vice president. He comes to us from Truckee Meadows Water Authority, where he served as general manager. Previously, Malyn was CEO of Sierra Pacific Resources and vice president of finance and treasurer at San Diego Gas and Electric. He replaces Jon E. Eliassen, who retired after nearly 33 years with Avista.

REGULATORY

- The Federal Energy Regulatory Commission (FERC) suspended its investigation of Avista after it found no evidence of improper energy trading practices.

Noxon Rapids Dam



- Montana voters resoundingly rejected Initiative 145 in the November general election. The defeat of the measure, which would have allowed the state to purchase a dozen privately owned hydroelectric dams, secures our continued ownership of the 527-megawatt Noxon Rapids Dam, our largest generation facility.

- Washington regulators allowed us to begin recovering $196 million in deferred power costs, approved a general rate case, and authorized an energy recovery mechanism to reduce our risk when market prices fluctuate.

ECONOMIC DEVELOPMENT

Scott L. Morris

- Scott L. Morris, senior vice president of Avista Corp. and president of Avista Utilities, was named chairman of the newly formed Washington State Economic Development Commission.

As we move Avista forward, certain principles guide our decisions: trust, integrity, innovation, relationships and collaboration. They are the means by which we will achieve our desired ends.

These are not unusual concepts, but the following pages will demonstrate how seriously we take them, how deeply we feel them, and how diligently we apply them.

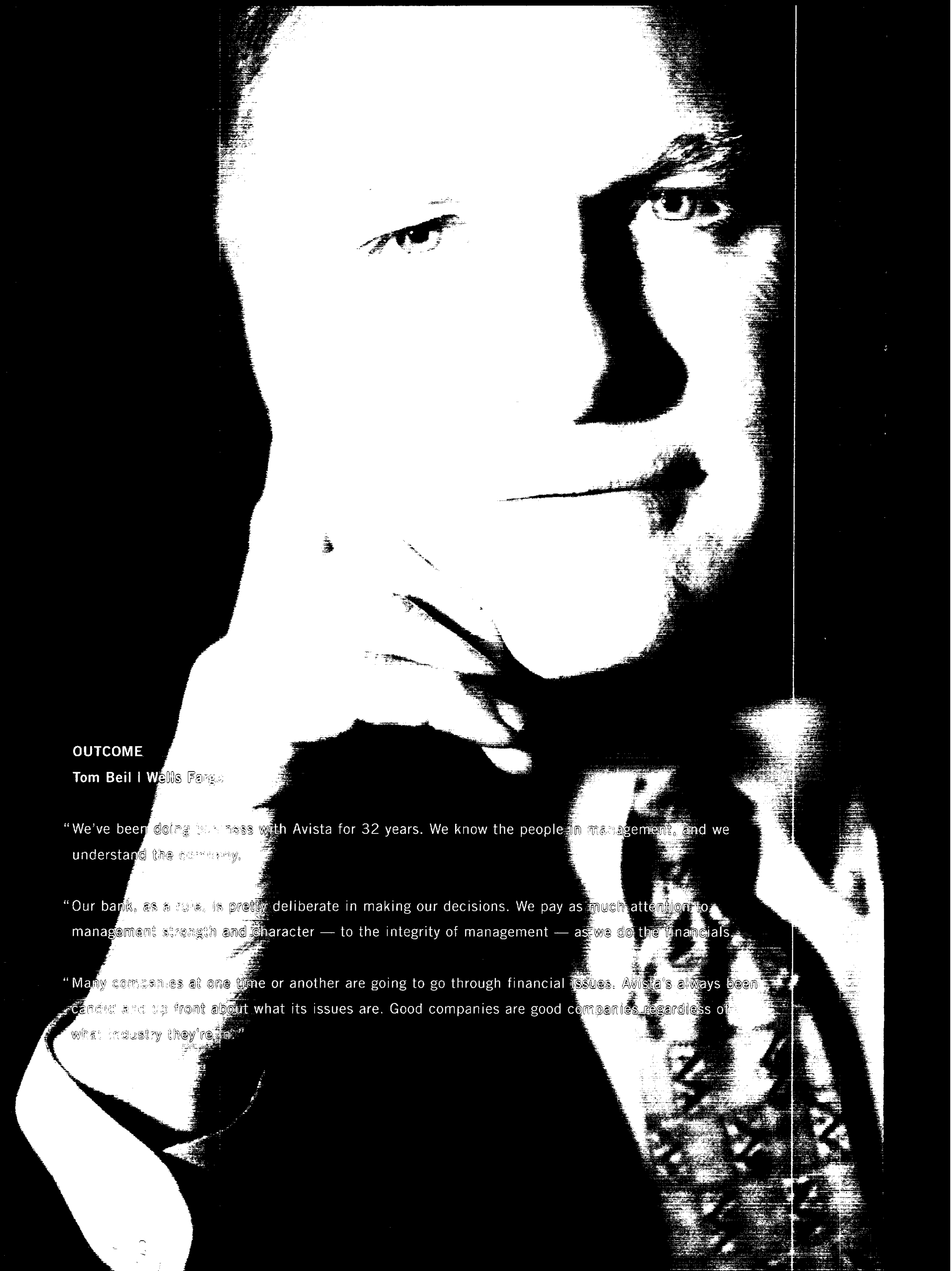
TRUST

INTEGRITY

INNOVATION

RELATIONSHIPS

COLLABORATION



OUTCOME

Tom Beil | Wells Fargo

"We've been doing business with Avista for 32 years. We know the people in management, and we understand the company.

"Our bank, as a rule, is pretty deliberate in making our decisions. We pay as much attention to management strength and character — to the integrity of management — as we do the financials.

"Many companies at one time or another are going to go through financial issues. Avista's always been candid and up front about what its issues are. Good companies are good companies regardless of what industry they're in."

Financial Responsibility

Doing the right thing in good times is fairly easy. Acting with integrity when times are tough shows a company's true mettle.

Last year, Wells Fargo and our other banks clearly observed how Avista deals with adverse conditions. We'd spent hundreds of millions of dollars to purchase power during the 2001 energy crisis. It was absolutely the correct decision — our customers have come to expect an exceptional level of reliability from us — but it had serious consequences that played out in 2002.

Others in our industry have experienced similar financial strains. We're not alone in that regard. But we think the way we dealt with those pressures was uniquely Avista.

First, we laid our cards on the table and sought counsel from those — like Wells Fargo — who know us best.

The costs we incurred jeopardized our credit agreements; we saw it coming and alerted our banks in advance. Those were frank and sometimes painful conversations, but they generated a level of trust that allowed our creditors the flexibility to waive some covenants while we addressed a series of challenging cash shortages and worked to regain our financial strength.

Then we made difficult, disciplined choices to bring capital expenditures and operating and maintenance expenses in under budget. We received rate increases to help drive down last year's energy deferral balances and lowered our debt ratio to 54 percent compared to 59 percent at the end of 2001.

We're determined to restore our bond rating to investment grade. While it may take a couple of years, we've seen progress already. In December, Standard & Poor's upgraded its credit outlook for Avista from negative to stable.

OPPORTUNITY:

Sharing Ideas

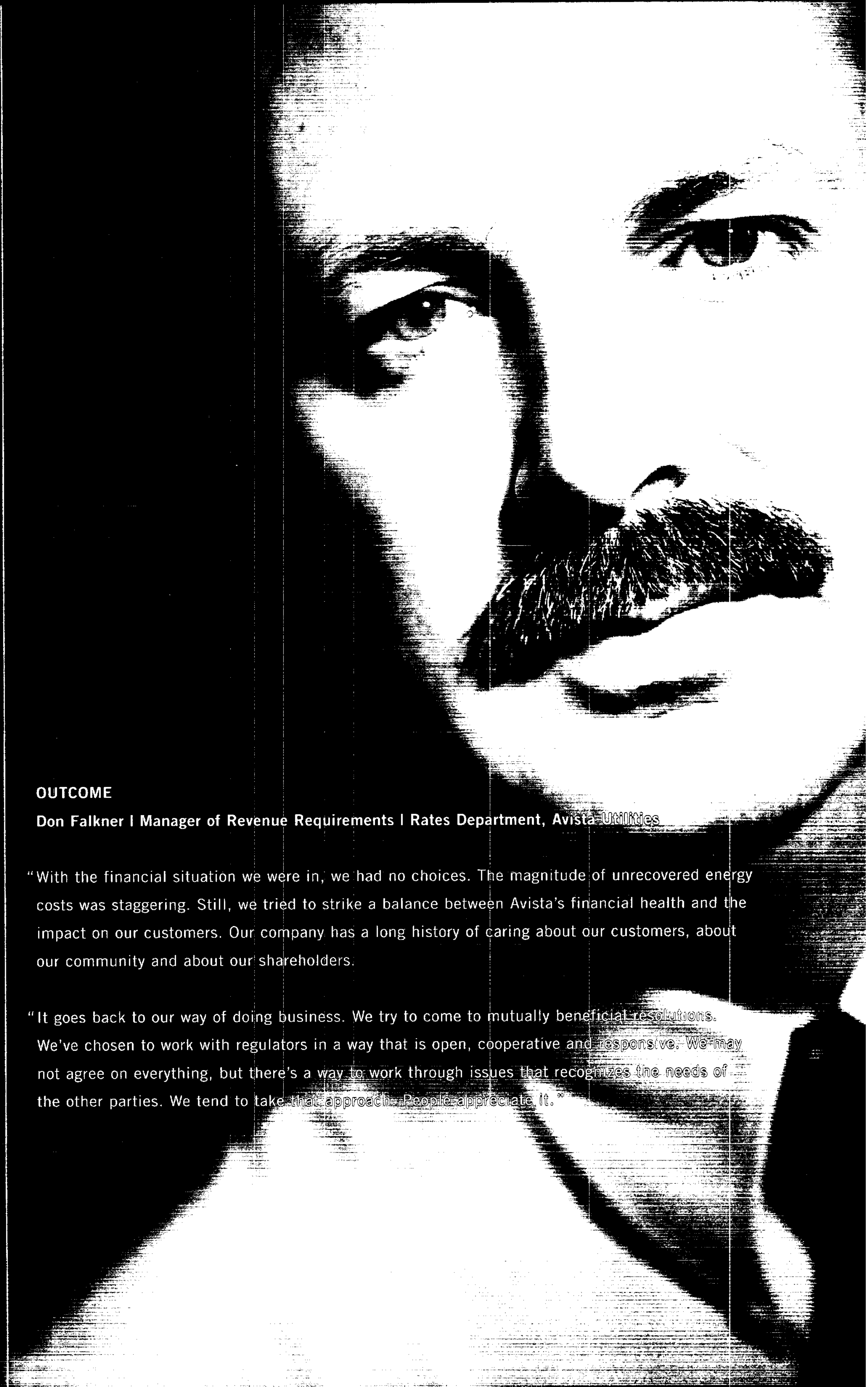
If ever a situation put our belief in collaboration to the test, this was it.

An unfortunate convergence of record low hydro conditions, a short supply of power and soaring wholesale prices led to the hundreds of millions of dollars in purchased power costs we'd incurred by the end of 2001. But by the middle of 2002, we'd successfully secured financial relief through an all-party settlement with Washington regulators and others involved in the case — and found a way to protect our customers' and shareholders' best interests in the process.

We'd previously been granted the right to recover 90 percent of our deferred power costs, and the final agreement included an energy recovery mechanism for adjusting electric rates up or down as necessary to reflect future changes in our supply costs. This mechanism will stabilize Avista's financial results in cases of severe market disruptions when prices spike. And by opting to spread our recovery of the deferred costs over time, we mitigate the financial effects on those we serve.

We recognize the benefits of such mutually agreeable resolutions, and we look for ways to bring them about. At Avista Energy, for instance, our five-year association with Clark County Public Utility District bears fruit for both parties. We gain experience in managing and transporting fuel for its gas-fired generation facility, and Clark County draws on our purchasing expertise. In another arrangement, we combine our understanding of the marketplace with Chelan County Public Utility District's aptitude for operating physical assets to meet demand with the right product — and maximize results.

We've always sought to collaborate with other players in the relatively new field of distributed generation. In 2002, Avista Labs formed a partnership with Airgas, Inc. for further developing the U.S. hydrogen-powered fuel cell market. We also established a supply agreement with 3M and three new distribution channels, including one for Italian markets with SGS Future s.r.l.



OUTCOME

Don Falkner | Manager of Revenue Requirements | Rates Department, Avista Utilities

"With the financial situation we were in, we had no choices. The magnitude of unrecovered energy costs was staggering. Still, we tried to strike a balance between Avista's financial health and the impact on our customers. Our company has a long history of caring about our customers, about our community and about our shareholders.

"It goes back to our way of doing business. We try to come to mutually beneficial resolutions. We've chosen to work with regulators in a way that is open, cooperative and responsive. We may not agree on everything, but there's a way to work through issues that recognizes the needs of the other parties. We tend to take that approach. People appreciate it."

OUTCOME

Martha Choe | Washington State Department of Community, Trade and Economic Development

"There are certain companies that integrate economic development with their business model. Avista is one of those companies.

"Scott Morris' participation in the governor's competitiveness council and his leadership in spearheading an economic development commission for the state both say a lot about the willingness of the company to step up and assume some responsibility. I think it demonstrates a real passion and a personal commitment on Scott's part to making sure the state is a great place to do business.

"It's a smart strategic move for Avista. For a utility to grow and thrive it needs more people, more businesses to serve. It's smart to find ways to grow the economy and find more customers."

OPPORTUNITY:

Economic Expansion

When Washington Governor Gary Locke asked Scott Morris, Avista senior vice president, to head the Washington State Economic Development Task Force, Scott didn't hesitate. Our deeply rooted tradition of working for the prosperity of the communities we serve made this a perfect fit for the company. And with his experience in a similar capacity in Oregon, it was a natural for Scott, too.

The task force's work led to the formation of a permanent state Economic Development Commission, and Scott has taken on the leadership of that group, as well.

Avista is drawn to this kind of public-private partnership. That's why we lent an Avista executive to the City of Spokane in 2002 to support the mayor and city council in their economic development activities. We also united with area developers to turn an old downtown hotel into a 35,000-square-foot office complex, and opened our high-speed fiber system to the region's education community, creating the Virtual Possibilities Network. Over the next five years, regional higher education institutions will have the opportunity to use our infrastructure for projects that focus on incubation, education, and research and development.

By bringing our strongest resources to bear in such collaborative efforts, we can truly effect change — and all reap the benefits of a healthy economy.

OPPORTUNITY:

Keeping Our Word

Given our predisposition toward reliability and low-cost service, choosing to expand our generation capacity was a relatively straightforward decision. Executing that decision, however, has presented some challenges.

After several technical equipment setbacks far beyond our control, our Coyote Springs 2 combined-cycle, natural gas generation plant near Boardman, Oregon, is expected to go on line in mid-2003. The team overseeing construction of the 280-megawatt facility that we own jointly with Mirant has endured a transformer fire, a subsequent oil spill, shipping damage to the replacement transformer and the bankruptcy of two key contractors.

In the end, Avista took on the role of general contractor, assumed the financial obligations of the previous contractors, made every effort to establish continuity with remaining employees and continued to forge ahead.

Of all our assets — including equipment, pipes and wires, and generation facilities — nothing's more valuable than our word. So when we can't deliver on a commitment, the first thing to do is own up. We meant to complete Coyote Springs 2 in 2002. It didn't happen. And we believe we should say so.

The importance we place on trustworthiness worked to our advantage when Avista Energy's credit agreement expired in June. Our new line of credit represents a $13 million increase over the previous line, a significant accomplishment considering the turmoil in energy markets. We take it as a much-appreciated vote of confidence from our banks.

OUTCOME

Tim Carlberg | Coyote Springs 2 Project Manager, Avista Utilities

"We work hard to build and sustain good relationships. People feel they can trust us. Not that we don't have bumpy roads sometimes, yet people at Avista can sleep at night knowing we've done the right thing.

"When we had the oil spill, we mobilized immediately. We had the Department of Environmental Quality on-site; we listened to them and supported them. In the end, the harm to the environment was zero. As an extra precaution, we handled this mineral oil as if it were hazardous waste, and yet it wasn't. Our monitoring wells are showing 'non-detect' levels and there's absolutely no oil on the water or the shorelines of the nearby pond. It was the best thing to do for the environment."

OUTCOME

Ann Carey I Associate Vice President of Sales, Avista Advantage

"The main thing that keeps customers with us through rocky times in the energy industry is the relationship we have built with them. Each of our teams has a core group of customers they work with so they know each other very well. We become an extension of the customer's company.

"Providing great service also serves us well. Our customers give us a lot of referrals, and we still have huge potential to up-sell to current customers. There's a lot of growth potential.

"To achieve and sustain profitability, we need to increase revenues and drive down costs. We're on a good track with both."

Controlling Costs

We're all for good ideas. But they must be profitable. So we've devoted considerable energy to turning a great product — utility bill processing and facility information management — into a solid contributor. And there's real progress to show for our efforts.

Today, it costs half what it cost last year for Avista Advantage to process an invoice. Twenty percent fewer employees handle 30 percent more bills. And we've improved gross margins from 9 percent in 2001 to 51 percent in 2002, generating our first-ever break-even cash flow this past November.

We've achieved those improvements through reduced costs, restructured business processes and more effective use of technology. These operational efficiencies leave our standard of service unchanged, though, and we've clearly earned our customers' loyalty — as the year's increased revenue attests.

At the corporate level, Avista instituted a hiring freeze, reductions in staff and aggressive budget cuts. That cost-conscious approach is not likely to change any time soon; our 2003 budgets will compensate for much higher pension, insurance and health-care costs. And although our utility customers continue to enjoy some of the lowest-priced electricity in the country, their bills are higher as a reflection of our increased operating costs.

While we can't control external business and economic circumstances, we can control our response. We've involved employees in addressing our financial issues, and we conducted a benchmark study to identify further strategic cost reductions.

OPPORTUNITY:

Real Connections

Certain opportunities call for a restrained response. Our regional marketing and trading company, Avista Energy, represents such a case. We've narrowed the scope and risk of this subsidiary's operations over the last few years, and it's proven the prudent course. Avista Energy's solid performance of 11 consecutively profitable quarters has contributed significantly to the corporation's overall financial health.

That record of success can be attributed, in large part, to strong, longstanding relationships with partners and customers such as Chelan County and Clark County Public Utility Districts. Avista also shares ownership of the Lancaster combined-cycle combustion turbine generating station in Idaho with Cogentrix Energy, Inc.; Avista Energy manages the fuel input and markets the entire 270-megawatt output through a long-term, power-purchase agreement. Alliances like these advance our strategy of extracting the most value from our energy assets and creating tailored packages for our customers. And they exemplify our firm conviction that respectful relationships are good business. A single statistic from another of our subsidiaries demonstrates the power of this idea.

When you achieve a 95 percent customer retention rate — as Avista Advantage has — you know you're treating people right. Our clients at KayBee Toys, for instance, faced the choice of upgrading their service or finding another provider. They shopped around, and in the end decided no other vendor understood their business or respected their needs the way Avista Advantage does.

Our relationship with Mirant, our Coyote Springs 2 partner, is another example. After we lost a general contractor during construction, Mirant felt enough confidence in our team to affirm our position in the lead role. This solution, reached in adversity, kept us moving forward cost-effectively.

OUTCOME

Jiong Ji | Senior Analyst, Avista Energy

"We concentrate on what we're good at. Experience is vital to any successful marketing company, and we have extensive background in the Western market. In other regions, there's more fixed generation and it's somewhat predictable. There are more variables in the Western energy market because hydro levels change quite a bit from one year to another. That's where our experience comes in.

"We use that experience to manage and optimize assets — like the Lancaster gas generation plant — and market the output. We also manage part of the Jackson Prairie gas storage facility in southwest Washington. And through an alliance with Chelan County Public Utility District, we share knowledge and uncover opportunities we might not find on our own. These arrangements are good for everybody."

OUTCOME

Arnette Daniels | Dispatcher, Avista Utilities

"Our outage management system has enormous potential. It actually tells us how many customers are on the line that's out. All the information the crews need is right at our fingertips.

"It's a great communication tool, too. Customers can call us for immediate updates on an outage. And it's going to give us information about our delivery system that will help us keep it in better working order.

"Avista trusts employees to find a better way to do things."

Breaking New Ground

Few businesses could survive as long as Avista has without plenty of enthusiasm for innovation.

When our employees decided customers would benefit from a new outage management tool, they took on the job themselves. Avista's people collaborated with the city and county, securing grid maps for a computerized geographic information system. The result — introduced in 2001 and enlarged in 2002 — speeds outage response times, prioritizes crew deployments, and links to our interactive voice response system to keep customers informed.

We appreciate employee-driven initiatives like the outage management tool. It's one way we find new, productive ways to take care of our customers, a goal that will become more and more important as we expand our customer base. Over the next four years, we anticipate our retail electric and gas sales to increase by up to four percent annually.

Natural gas, in particular, holds potential for growth. A survey of our natural gas customers in four states found an average of 2.5 burner tips per household, while new construction sites average 3.4 burner tips. Each burner tip represents a natural-gas-operated device such as a fireplace, stove or other appliance.

Another service introduced in 2002 offers customers the option of purchasing wind power. The program extends our activities in alternative energy beyond Avista Labs' fuel cell technology. We also worked with a partner company to launch Avista Connections in 2002, a free service for our residential customers. With one call, a customer can set up local phone, long distance, cable television, newspaper delivery and Avista Utilities services.

INDEPENDENT AUDITORS' REPORT

Avista Corporation
Spokane, Washington

We have audited the consolidated balance sheets and the statements of capitalization of Avista Corporation and subsidiaries (the Company) as of December 31, 2002 and 2001, and the related consolidated statements of income and comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2002. Such consolidated financial statements and our report thereon dated February 7, 2003, (March 3, 2003, as to Note 28) expressing an unqualified opinion (which are not presented herein), are included in Appendix A to the 2002 annual report. The accompanying condensed consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on such condensed consolidated financial statements in relation to the complete consolidated financial statements.

In our opinion, the information set forth in the accompanying condensed consolidated balance sheets as of December 31, 2002 and 2001, and the related condensed consolidated statements of income and cash flows for each of the three years in the period ended December 31, 2002, is fairly stated in all material respects in relation to the basic consolidated financial statements from which it has been derived.

As described in Note 2 to the consolidated financial statements included in Appendix A to the 2002 annual report, during 2002, the Company changed its method of accounting for goodwill to conform to Statement of Financial Accounting Standards No. 142, also, the Company changed its presentation of energy trading activities in accordance with Emerging Issues Task Force Issue No. 02-3.

Deloitte + Touche LLP

Seattle, Washington
February 7, 2003
(March 3, 2003, as to the information derived from Note 28 to the consolidated financial statements.)

MANAGEMENT'S STATEMENT OF RESPONSIBILITY

The condensed consolidated financial statements in this summary annual report were derived from the consolidated financial statements that appear in Appendix A to the 2002 annual report. Management of Avista Corporation is responsible for the accuracy and completeness of the information in this summary annual report. The financial and operating information is derived from company records, and includes amounts based on judgment and estimates where necessary. Quality control practices for reporting business information in combination with the company's internal control procedures provide adequate assurance that the summary annual report fairly and reasonably presents the company's financial position and operating results.

The board of directors appointed Deloitte & Touche LLP, an independent accounting firm, to audit the consolidated financial statements included in Appendix A to the 2002 annual report. Their report on the condensed consolidated financial statements appears above.

Gary G. Ely
Chairman, President and
Chief Executive Officer

Malyn K. Malquist
Senior Vice President and
Chief Financial Officer

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(For the Years Ended December 31 — Dollars in Thousands, Except Per Share Amounts)	2002	2001	2000
Operating Revenues	$ 980,446	$1,395,313	$1,858,516
Operating Expenses			
Resource costs	453,525	849,996	1,246,459
Operations and maintenance	122,920	125,656	129,708
Administrative and general	118,766	119,216	134,912
Depreciation and amortization	73,275	71,981	65,936
Taxes other than income taxes	67,273	59,172	54,608
Restructuring and exit costs	—	—	9,805
Total operating expenses	835,759	1,226,021	1,641,428
Income from Operations	144,687	169,292	217,088
Other Income (Expense)			
Interest expense	(105,336)	(106,480)	(68,255)
Capitalized interest	7,486	10,498	3,359
Net interest expense	(97,850)	(95,982)	(64,896)
Other income — net	17,467	20,681	25,861
Total other income (expense) — net	(80,383)	(75,301)	(39,035)
Income from Continuing Operations before Income Taxes	64,304	93,991	178,053
Income Taxes	29,994	34,386	76,998
Income from Continuing Operations	34,310	59,605	101,055
Income (Loss) from Discontinued Operations	1,145	(47,449)	(9,376)
Net Income before Cumulative Effect of Accounting Change	35,455	12,156	91,679
Cumulative Effect of Accounting Change	(4,148)	—	—
Net Income	31,307	12,156	91,679
Deduct — Preferred Stock Dividend Requirements	2,402	2,432	23,735
Income Available for Common Stock	$ 28,905	$ 9,724	$ 67,944
Earnings per Common Share, Basic			
Earnings per common share from continuing operations	$ 0.67	$ 1.21	$ 1.69
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.21	1.49
Loss per common share from cumulative effect of accounting change	(0.09)	—	—
Total earnings per common share, basic	$ 0.60	$ 0.21	$ 1.49
Earnings per Common Share, Diluted			
Earnings per common share from continuing operations	$ 0.67	$ 1.20	$ 1.67
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.20	1.47
Loss per common share from cumulative effect of accounting change	(0.09)	—	—
Total earnings per common share, diluted	$ 0.60	$ 0.20	$ 1.47
Dividends paid per common share	$ 0.48	$ 0.48	$ 0.48

CONDENSED CONSOLIDATED BALANCE SHEETS

(As of December 31 — Dollars in Thousands)	2002	2001
Assets		
Current energy commodity assets	$ 365,477	$ 477,037
Other current assets	603,245	655,980
Total net utility property	1,563,704	1,565,642
Investment in exchange power — net	40,833	43,314
Nonutility properties and investments — net	204,522	230,800
Noncurrent energy commodity assets	348,309	383,497
Other property and investments — net	12,702	13,620
Regulatory assets for deferred income tax	139,138	149,033
Other regulatory assets	29,735	192,760
Utility energy commodity derivative assets	60,322	1,889
Power and natural gas deferrals	166,782	265,063
Other deferred charges	79,364	58,588
Total Assets	$3,614,133	$4,037,223
Liabilities and Capitalization		
Current energy commodity liabilities	$ 304,781	$ 373,837
Current portion of long-term debt	71,901	1,827
Short-term borrowings	30,000	75,099
Other current liabilities	534,148	477,711
Noncurrent energy commodity liabilities	314,204	299,980
Deferred income taxes	454,147	517,428
Utility energy commodity derivative liabilities	50,058	159,418
Other noncurrent liabilities and other deferred credits	106,218	101,145
Capitalization:		
Long-term debt	902,635	1,175,715
Preferred trust securities	100,000	100,000
Preferred stock	33,250	35,000
Common stock — net (48,044,208 and 47,632,678 outstanding shares)	607,018	600,134
Retained earnings and accumulated other comprehensive loss	105,773	119,929
Total capitalization	1,748,676	2,030,778
Total Liabilities and Capitalization	$3,614,133	$4,037,223

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash and Cash Equivalents (For the Years Ended December 31 — Dollars in Thousands)	2002	2001	2000
Continuing Operating Activities:			
Net income	$ 31,307	$ 12,156	$ 91,679
Loss (income) from discontinued operations	(1,145)	47,449	9,376
Cumulative effect of accounting change	4,148	—	—
Noncash items included in net income:			
Depreciation and amortization	73,275	71,981	65,936
Provision for deferred income taxes	(40,287)	79,141	79,274
Power and natural gas cost amortizations (deferrals), net	68,481	(210,540)	(70,250)
Energy commodity assets and liabilities	87,403	30,238	(174,680)
Other	(1,902)	1,783	(29,061)
Changes in working capital components	110,038	(108,278)	111,816
Net Cash Provided by (Used in) Continuing Operating Activities	331,318	(76,070)	84,090
Continuing Investing Activities:			
Utility property construction expenditures (excluding AFUDC)	(64,207)	(119,905)	(98,680)
Other capital expenditures	(19,390)	(162,279)	(73,515)
Changes in other property and investments	35,190	11,163	3,403
Proceeds from property sales and sale of subsidiary investments	586	75,953	105,228
Assets acquired and investments in subsidiaries	(461)	(23,321)	(1,496)
Net Cash Used in Continuing Investing Activities	(48,282)	(218,389)	(65,060)
Continuing Financing Activities:			
Increase (decrease) in short-term borrowings	(45,099)	(88,061)	42,126
Increase (decrease) in long-term debt	(203,393)	410,249	169,717
Redemption of preferred trust securities and preferred stock	(1,750)	—	(10,000)
Issuance of common stock	7,035	8,267	4,532
Cash dividends paid	(25,456)	(25,110)	(28,304)
Other	(15,990)	(19,693)	(2,757)
Net Cash Provided by (Used in) Continuing Financing Activities	(284,653)	285,652	175,314
Net Cash Provided by (Used in) Continuing Operations	(1,617)	(8,807)	194,344
Net Cash Provided by (Used in) Discontinued Operations	16,765	(17,210)	(37,094)
Net Increase (Decrease) in Cash and Cash Equivalents	15,148	(26,017)	157,250
Cash and Cash Equivalents at Beginning of Period	171,221	197,238	39,988
Cash and Cash Equivalents at End of Period	$ 186,369	$ 171,221	$ 197,238

FINANCIAL SUMMARY

The following is a brief discussion and analysis of financial condition and results of operations for 2002. For a more detailed analysis, please refer to Appendix A to the 2002 annual report.

Overall Results of Operations – Income from continuing operations was $34.3 million for 2002 compared to $59.6 million for 2001. The decrease was primarily due to reduced net income recorded by the Energy Trading and Marketing line of business. Energy Trading and Marketing recorded net income of $0.47 per share in 2002 compared to $1.33 per share in 2001. Net income recorded by Avista Utilities was $0.71 per share in 2002, compared to $0.46 per share in 2001. The Information and Technology line of business incurred a net loss of $0.25 per share in 2002 compared to $0.41 per share in 2001. The Other line of business incurred a net loss of $0.26 per share in 2002 compared to $0.18 per share in 2001. The discontinued operations of Avista Communications recorded net income of $0.02 per share in 2002 compared to a net loss of $1.00 per share in 2001.

In April 2002, the Company completed its transitional test of goodwill related to the adoption of Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." Accordingly, the Company determined that $6.4 million of goodwill, related to a subsidiary in the Other business segment, was impaired. The Company recorded this impairment of $4.1 million, net of tax, or $0.09 per share, as a cumulative effect of accounting change.

Avista Utilities – Avista Utilities recorded net income of $36.4 million for 2002 compared to $24.2 million for 2001. Avista Utilities' income from operations was $149.2 million for 2002 compared to $114.9 million for 2001. This increase was primarily due to an increase in gross margin (operating revenues less resource costs). Avista Utilities' operating revenues decreased $336.9 million and resource costs decreased $396.5 million resulting in an increase of $59.6 million in gross margin for 2002 as compared to 2001. The increase in gross margin was partially offset by an increase in administrative and general expenses, depreciation and amortization and taxes other than income taxes. The general electric rate increase of 19.3 percent in Washington base retail rates effective July 1, 2002, contributed to the increase in gross margin.

Retail electric revenues increased $65.2 million for 2002 from 2001. This increase was primarily due to the electric surcharges implemented to recover deferred power costs and the June 2002 Washington electric rate increase, partially offset by decreased use per customer and total kWhs sold. The increase in retail electric revenues was also due to refunds to customers in January 2001 of the gain on the sale of Avista Utilities' interest in the Centralia Power Plant that reduced revenues for 2001. Wholesale electric revenues decreased $416.8 million, or 87 percent, reflecting wholesale sales volumes which decreased 65 percent from 2001 and average sales prices that were 62 percent lower than the prior year. Wholesale sales volumes decreased primarily due to the expiration of several wholesale electric sales contracts, including two 100 MW index-based sales contracts that expired in July 2001. The extent of future wholesale transactions will be based on the availability of resources owned or controlled by Avista Utilities and changes to loads of Avista Utilities' customers and contractual obligations.

Other electric revenues increased $13.5 million primarily due to the sale of natural gas purchased for electric generation that was not used in generation. Avista Utilities operated less thermal generation in 2002 as compared to 2001 based on lower retail demand, increased hydroelectric generation and decreased wholesale market prices.

Natural gas revenues increased $1.2 million for 2002 from 2001 due to a slight increase in retail and transportation revenues, partially offset by a decrease in wholesale natural gas revenues. Retail rates were increased during 2001 to recover deferred natural gas costs. During the fourth quarter of 2002, retail rates for natural gas were reduced in response to a decrease in current and projected natural gas costs.

Power purchased for 2002 decreased $593.0 million, or 84 percent, compared to 2001 due to the decreased volume and price of power purchases. Average purchased power prices for 2002 were 68 percent lower than 2001 and volumes purchased decreased 49 percent compared to 2001. The decrease in the volume of purchased power was primarily the result of decreases in the volume of wholesale electric sales and increased hydroelectric resource availability to meet retail demand.

Net amortization of deferred power costs was $26.3 million in 2002 compared to net deferrals of $202.8 million in 2001. During 2002, Avista Utilities recovered (collected as revenue) $38.6 million of previously deferred power costs in Washington and $24.7 million in Idaho. During 2002, Avista Utilities deferred $22.4 million of power costs in Washington and $13.5 million in Idaho. During 2002, $27.7 million of a deferred credit was offset against the Idaho share of deferred power costs. Total deferred power costs were $155.3 million as of December 31, 2002.

During 2002, Avista Utilities had $42.2 million of net amortization of deferred natural gas costs, compared to net deferrals of $7.7 million in 2001. Total deferred natural gas costs were $11.5 million as of December 31, 2002.

The cost of fuel for generation for 2002 decreased $63.4 million from 2001 primarily due to a decrease in thermal generation as well as a decrease in the average cost of natural gas used for generation. Thermal generation decreased 43 percent primarily due to increased hydroelectric generation and wholesale market prices that were generally below the cost of operating the thermal generating units.

The expense for natural gas purchased for 2002 decreased $50.0 million compared to 2001 primarily due to the decreased average cost of natural gas.

Other fuel costs for 2002 increased $34.6 million compared to 2001. This was due to an increase in natural gas purchased as fuel for electric generation that was not used. This excess natural gas was sold with the associated revenues reflected as other electric revenues.

2002 FINANCIAL REPORT

APPENDIX A

AVISTA
Corp.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

Safe Harbor for Forward-Looking Statements

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

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

- changes in the utility regulatory environment in the individual states in which the Company operates and the United States in general. This can impact allowed rates of return, financings, or industry and rate structures;
- the impact of regulatory and legislative decisions including Federal Energy Regulatory Commission (FERC) price controls, and including possible retroactive price caps and resulting refunds;
- the impact from the potential formation of a Regional Transmission Organization and/or an Independent Transmission Company;
- the impact from the implementation of the FERC's proposed Standard Market Design;
- the availability and prices of purchased energy, volatility and illiquidity in wholesale energy markets;
- wholesale and retail competition (including but not limited to electric retail wheeling and transmission costs);
- future streamflow conditions that affect the availability of hydroelectric resources;
- outages at any company-owned generating facilities;
- unanticipated delays or changes in construction costs with respect to present or prospective generating facilities;
- changes in weather conditions that can affect customer demand, result in natural disasters and/or customer outages, and affect the availability of hydroelectric resources;
- changes in industrial, commercial and residential growth and demographic patterns in the Company's service territory;
- the loss of significant customers and/or suppliers;
- failure to deliver on the part of any parties from which the Company purchases and/or sells capacity or energy;
- changes in the creditworthiness of customers and energy trading counterparties;
- the Company's ability to obtain financing through the issuance of debt and/or equity securities, which can be affected by various factors including the Company's credit ratings, interest rate fluctuations and other capital market conditions;
- changes in future economic conditions in the Company's service territory and the United States in general, including inflation or deflation and monetary policy;
- the continuing impact of the September 11, 2001 terrorist attacks as well as the potential for future terrorist attacks, particularly with respect to utility plant assets;
- changes in tax rates and/or policies;
- research and development findings for the Information and Technology companies;
- changes in, and compliance with, environmental and endangered species laws, regulations, decisions and policies, including present and potential environmental remediation costs;
- the outcome of legal and regulatory proceedings concerning the Company or affecting directly or indirectly its operations;
- employee issues, including changes in collective bargaining unit agreements, strikes, work stoppages or the loss of any of the Company's key executives;
- changes in actuarial assumptions and the return on assets with respect to the Company's pension plan, which can impact future funding obligations, costs and pension plan liabilities;
- increasing health care costs and the resulting effect on health insurance premiums paid for employees and the

obligation to provide postretirement health care benefits;
- increasing costs of insurance and the ability to obtain insurance.

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

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

Avista Corp. Lines of Business

Avista Corp. is an energy company engaged in the generation, transmission and distribution of energy as well as other energy-related businesses. The Company is organized into four lines of business – Avista Utilities, Energy Trading and Marketing, Information and Technology, and Other. Avista Utilities, an operating division of Avista Corp. and not a separate entity, represents the regulated utility operations. Avista Capital, a wholly owned subsidiary of Avista Corp., is the parent company of all of the subsidiary companies engaged in the non-utility lines of business. As of December 31, 2002, the Company had common equity investments of $457.6 million and $255.2 million in Avista Utilities and Avista Capital, respectively.

Avista Utilities generates, transmits and distributes electricity and distributes natural gas. Avista Utilities owns and operates eight hydroelectric projects, a wood-waste fueled generating station, a two-unit natural gas-fired combustion turbine (CT) generating facility and two small generating facilities. It also owns a 15 percent share in a two-unit coal-fired generating facility and leases and operates a two-unit natural gas-fired CT generating facility. At the end of 2002, Avista Utilities' facilities had a total net capability of approximately 1,511 megawatts (MW), of which 64 percent was hydroelectric and 36 percent was thermal. In mid-2003, it is expected that the natural gas-fired Coyote Springs 2 Generation Project (Coyote Springs 2) will be placed into operation. Avista Utilities has a 50 percent ownership interest (140 MW) in Coyote Springs 2.

In addition to company owned resources, Avista Utilities has a number of long-term power purchase and exchange contracts that increase its available resources. Avista Utilities sells and purchases electric capacity and energy to and from utilities and other entities in the wholesale market under long-term contracts having terms of more than one year. In addition, Avista Utilities engages in an ongoing process of resource optimization which involves short-term purchases and sales in the wholesale market in pursuit of an economic selection of resources to serve retail and wholesale loads. Avista Utilities makes continuing projections of (1) future retail and wholesale loads based on, among other things, forward estimates of factors such as customer usage and weather as well as historical data and contract terms and (2) resource availability based on, among other things, estimates of streamflows, generating unit availability, historic and forward market information and experience. On the basis of these continuing projections, Avista Utilities makes purchases and sales of energy on an annual, quarterly, monthly, daily and hourly basis to match actual resources to actual energy requirements. This process includes hedging transactions.

The Energy Trading and Marketing line of business is comprised of Avista Energy, Inc. (Avista Energy) and Avista Power, LLC (Avista Power). Avista Energy is an electricity and natural gas marketing and trading business, operating primarily in the Western Electricity Coordinating Council (WECC) geographical area, which is comprised of eleven Western states. Avista Power was originally formed to develop and own generation assets. During 2001, the Company decided that Avista Power would no longer pursue the development of additional non-regulated generation projects.

The Information and Technology line of business is comprised of Avista Advantage, Inc. (Avista Advantage) and Avista Laboratories, Inc. (Avista Labs). Avista Advantage is a provider of internet-based facility intelligence, cost management, billing and information services to retail customers throughout North America. Its primary product lines include consolidated billing, resource accounting, energy analysis, load profiling and maintenance and repair billing services. Avista Labs has patented and developed a modular air-cooled, self-hydrating Proton Exchange Membrane (PEM) fuel cell that delivers reliable and clean distributed power solutions. In addition to developing its modular fuel cell products, Avista Labs is contracting with selected market channels to deliver system solutions to industrial, commercial and residential markets. Avista Labs holds a 70 percent equity interest in H2fuel, LLC, a developer of fuel processors for the production of hydrogen. Avista Corp. is currently seeking a financial partner for Avista Labs with the goal of reducing its ownership interest to less than 20 percent of this company.

The Other line of business includes several subsidiaries, including Avista Ventures, Inc. (Avista Ventures), Avista Capital (parent company only amounts), Pentzer Corporation (Pentzer), Avista Development and Avista Services. The Company continues to limit its future investment in this line of business.

Avista Communications, Inc. (Avista Communications), formerly part of the Information and Technology line of business, provided local dial tone, data transport, internet services, voice messaging and other telecommunications services to several communities in the western United States. In September 2001, Avista Corp. decided that it would dispose of substantially all of the assets of Avista Communications. As such, these operations are reported as a discontinued operation. Avista Corp. began its divestiture of this business during the fourth quarter of 2001, and the divestiture of operating assets was complete by the end of 2002. Certain liabilities of the operations remain to be settled.

Avista Utilities – Regulatory Matters

Beginning in the second quarter of 2000, the price of power in the wholesale markets of the western United States increased considerably and became much more volatile. While prices and volatility decreased during the second half of 2001, the effects of contracts entered into during the period of high wholesale prices continue to have an impact on Avista Corp.'s financial condition, results of operations and cash flows. In the second half of 2000 and continuing through 2001, Avista Utilities was required to purchase above-normal amounts of power in the wholesale market to meet its retail demand. This was primarily due to the reduced availability of hydroelectric resources as a result of low streamflow conditions. The combination of high wholesale market prices and increased amounts required to be purchased increased power supply costs to amounts far in excess of the amounts recovered from retail customers under rates in effect at the time.

The Company has had a power cost deferral mechanism in place in Washington as authorized by the Washington Utilities and Transportation Commission (WUTC) since the middle of 2000. The Company has had a power cost deferral mechanism in place in Idaho as authorized by the Idaho Public Utilities Commission (IPUC) since 1989. Avista Utilities defers the recognition in the income statement of certain power supply costs that are in excess of the level currently recovered from retail customers. A portion of power supply costs are recorded as a deferred charge on the balance sheet for future review and the opportunity for recovery through retail rates. The specific power costs deferred are a percentage of the difference between certain actual power supply costs incurred by Avista Utilities and the costs included in base retail rates. This difference is primarily related to changes in short-term wholesale market prices, changes in the level of hydroelectric generation and changes in the level of thermal generation (including changes in fuel prices). Avista Utilities accrues interest on deferred power costs in the Washington jurisdiction at a rate, which is adjusted semi-annually, of 8.9 percent as of December 31, 2002. Avista Utilities accrues interest on deferred power costs in the Idaho jurisdiction at a rate, which is adjusted annually, of 2 percent as of December 31, 2002. Avista Utilities anticipates making a filing with the IPUC requesting that the interest rate be modified to more closely approximate Avista Utilities' costs of short-term borrowings until the current surcharge is eliminated.

In June 2002, the WUTC issued an order that became effective July 1, 2002 with respect to a general electric rate case filed by Avista Utilities in December 2001. The order provides for an overall rate of return of 9.72 percent and a return on equity of 11.16 percent. The order provided for no incremental rate increase to Avista Utilities' Washington electric customers above the rates in effect at the time. Rate increases previously approved by the WUTC totaling 31.2 percent (a 25 percent temporary surcharge approved in September 2001 for the recovery of deferred power costs and a 6.2 percent increase approved in March 2002) were restructured. The general increase to base retail rates is 19.3 percent (or $45.7 million in expected annual revenues) and the remaining 11.9 percent represents the continued recovery of deferred power costs over a period currently projected to continue into 2009.

In the June 2002 rate order, the WUTC approved the establishment of an Energy Recovery Mechanism (ERM). The ERM replaced a series of temporary power cost deferral mechanisms that were in place in Washington since mid-2000. The ERM allows Avista Utilities to increase or decrease electric rates periodically with WUTC approval to reflect changes in power supply costs. The ERM provides for Avista Utilities to incur the cost of, or receive the benefit from, the first $9 million in annual power supply costs above or below the amount included in base retail rates. Under the ERM, 90 percent of the power supply costs exceeding or below the initial $9 million will be deferred for future surcharge or rebate to Avista Utilities' customers. The remaining 10 percent will be an expense of, or benefit to, the Company. Because the ERM was implemented on July 1, 2002, the Company's expense or benefit was limited to $4.5 million plus the remaining 10 percent of all costs above the amount included in base retail rates for 2002.

The Company expensed the initial $4.5 million in power supply costs above the amount included in base retail rates plus 10 percent of all costs exceeding the initial $4.5 million under the ERM during 2002. The Company currently expects to expense the first $9 million of power supply costs above the amount included in base retail rates under the ERM during the first quarter of 2003 as well as 10 percent of any costs exceeding the first $9 million for the year of 2003. The Company also expects to expense the first $9 million of power supply costs above the amount included in base retail rates in 2004 as well as 10 percent of any costs exceeding the first $9 million. The majority of these costs relate to fuel contracts entered during 2001 that expire in 2004 for the Company's thermal generating units.

Avista Utilities has a power cost adjustment (PCA) mechanism in Idaho that allows it to modify electric rates periodically with IPUC approval to recover or rebate a portion of the difference between actual and allowed net power supply costs. The PCA mechanism allows for the deferral of 90 percent of the difference between certain actual net power supply expenses and the authorized level of net power supply expense approved in the last Idaho general rate case. In October 2002, the IPUC issued an order extending a 19.4 percent PCA surcharge for Idaho electric customers. In the order, the IPUC removed $0.9 million of costs associated with three small generation projects from the PCA. The Company will have the opportunity to address the recovery of these costs in a future rate proceeding. The IPUC also ordered that $0.6 million in fuel costs would receive additional review as part of the next PCA filing. The PCA surcharge will remain in effect until October 2003. The IPUC directed Avista Utilities to file a status report 60 days before the current PCA surcharge expires. If review of the status report and the actual balance of deferred power costs support continuation of the PCA surcharge, the IPUC has indicated that it anticipates the PCA surcharge will be extended for an additional period.

The following table shows activity in deferred power costs for Washington and Idaho during 2001 and 2002 (dollars in thousands):

	Washington	Idaho	Total
Deferred power costs as of December 31, 2000	$34,580	$2,693	$37,273
Activity from January 1 – December 31, 2001:			
Power costs deferred	167,196	73,677	240,873
Unrealized loss on fuel contracts (1)	8,232	4,077	12,309
Interest and other net additions	16,027	5,643	21,670
Amortization of deferred credit	(53,794)	(6,927)	(60,721)
Recovery of deferred power costs through retail rates	(10,223)	(6,076)	(16,299)
Write-off deferred power costs	(21,780)	-	(21,780)
Deferred power costs as of December 31, 2001	140,238	73,087	213,325
Activity from January 1 – December 31, 2002:			
Power costs deferred	22,423	13,471	35,894
Unrealized gain on fuel contracts (1)	(7,068)	(3,485)	(10,553)
Interest and other net additions	6,726	888	7,614
Amortization of deferred credit	-	(27,711)	(27,711)
Recovery of deferred power costs through retail rates	(38,570)	(24,732)	(63,302)
Deferred power costs as of December 31, 2002	$123,749	$31,518	$155,267

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

During a year having normal streamflow conditions, Avista Utilities would expect to have generation from its hydroelectric resources (both owned and purchased under long-term hydroelectric contracts) of approximately 550 aMW. For 2002, streamflow conditions were 112 percent of normal and hydroelectric generation was 553 aMW (101 percent of normal). Hydroelectric generation for the year 2001 was 369 aMW (67 percent of normal), which was 181 aMW below normal and the lowest level in the 73 years in which records have been kept. Preliminary forecasts and snowpack conditions indicate streamflow conditions for 2003 are expected to be approximately 70 percent of normal. Avista Utilities currently estimates that hydroelectric generation will be 458 aMW (83 percent of normal) in 2003. Below normal hydroelectric generation will cause Avista Utilities to either increase its output from thermal generation resources or purchase energy in the wholesale market, or Avista Utilities will have less surplus energy available to sell in the wholesale market. The Company will choose the most appropriate cost-effective resources to meet its customer demand. Under the ERM and the PCA mechanism, 90 percent of any costs exceeding the first $9 million in Washington and 90 percent of any costs incurred above the amount included in base retail rates in Idaho will be deferred for future recovery. In each instance, the remaining 10 percent will be an expense to the Company. Based on current projections, total deferred power costs are expected to be approximately $166 million at the end of 2003.

Avista Utilities is currently planning to file a natural gas general rate case in Oregon during the first half of 2003. The Company regularly reviews the need for natural gas or electric rate changes in each state in which it provides service.

During the second half of 2002, Avista Utilities adjusted its natural gas rates in response to a decrease in current and projected natural gas costs. During the fourth quarter of 2002, natural gas rate decreases of 17.4 percent, 15.5 percent, 7.1 percent and 16.2 percent were approved and implemented in Washington, Idaho, Oregon and California, respectively. These natural gas rate decreases are designed to pass through changes in purchased natural gas costs to customers and reduce operating revenues and resource costs with no change in Avista Utilities' gross margin or net income. Total deferred natural gas costs were $11.5 million and $52.7 million as of December 31, 2002 and 2001, respectively.

Power Market Issues

Avista Utilities and Avista Energy participate directly and indirectly in the power markets in the United States. Developments in these markets, particularly in the western part of the United States, have affected both Avista Utilities and Avista Energy. Federal and state officials including, but not limited to, the FERC and the California Public Utility Commission (CPUC), commenced reviews in 2000 to determine the causes of the changes in the wholesale energy markets to develop legal and regulatory remedies to address alleged market failures or abuses and large defaults by certain parties in the wholesale markets. The proceedings are continuing and their ultimate outcome and the resulting impact on the Company cannot be predicted at this time.

California Energy Crisis

In early 2001, California's two largest utilities, Southern California Edison (SCE) and Pacific Gas & Electric Company (PG&E), defaulted on payment obligations owed to various energy sellers, including the California Power Exchange (CalPX), California Independent System Operator (CalISO), and Automated Power Exchange (APX). Consequently, CalPX, CalISO and APX defaulted on their payment obligations to Avista Energy. PG&E and CalPX filed voluntary petitions under chapter 11 of the bankruptcy code for protection from creditors. On March 1, 2002, SCE paid its past due obligations to the CalPX and various other creditors; however, these funds did not flow directly to Avista Energy. As of December 31, 2002, Avista Energy's accounts receivable outstanding related to defaulting parties in California did not exceed its reserves for uncollected amounts, cost of collection, and refunds. Avista Energy is currently pursuing recovery of the defaulted obligations. Reserves for defaulted payments established in 2000 and 2001 accounted for the majority of the Company's increase in the total allowance for doubtful accounts. The allowance for doubtful accounts was $46.9 million as of December 31, 2002 compared to $50.2 million as of December 31, 2001 and $14.4 million as of December 31, 2000.

In July 2001, the FERC issued an order to commence a fact-finding hearing to determine if refunds should be owed and, if so, the amounts of such refunds for sales during the period from October 2, 2000 to June 20, 2001 in the California spot market. The order provides that any refunds owed could be offset against unpaid energy debts due to the same party. However, the FERC announced that it is considering changing the method used to determine natural gas costs for calculating refunds in this proceeding, which could delay their findings. Furthermore, on November 20, 2002, the FERC issued a Discovery Order, which reopened the evidentiary record and allowed parties in the proceeding to conduct additional discovery for the period January 1, 2000 to June 20, 2001. The November 20, 2002 Discovery Order required that, by no later than March 3, 2003, the market participants provide relevant documents to support any proposed recommendations to the FERC. The Discovery Order also affords parties in this proceeding the opportunity to respond by March 20, 2003 to submissions made by March 3, 2003. On December 12, 2002, the FERC Administrative Law Judge issued a Certification of Proposed Findings on California Refund Liability detailing the proposed refund amounts, which was presented to the FERC for consideration.

Several parties filed documents with the FERC on March 3, 2003 presenting supplemental information regarding alleged improper market conduct and requests for refunds and other relief under the additional discovery procedures set forth in both the California and Pacific Northwest refund proceedings. The filing parties include the California Parties (a joint filing including the Attorney General of the State of California, the California Electricity Oversight

Board, the CPUC, and PG&E), the City of Tacoma and Port of Seattle (jointly), the City of Seattle, and the Washington State Attorney General. The filing parties, with the exception of the Washington State Attorney General, have made specific allegations with regard to many companies, including Avista Corp. and Avista Energy.

Avista Corp. and Avista Energy will file reply comments in response to the allegations of the parties by March 20, 2003. Based upon an initial review of the filings, there are no new allegations or information not known to and addressed by the FERC Trial Staff in a separate investigation of Avista Corp. and Avista Energy.

As explained at "Federal Energy Regulatory Commission Inquiry" in "Note 28 of the Notes to Consolidated Financial Statements" regarding the investigation of Avista Corp. and Avista Energy, the FERC Trial Staff concluded that: 1) There was no evidence that any executives or employees of Avista Utilities or Avista Energy knowingly engaged in or facilitated any improper trading strategy and 2) There was no evidence that Avista Utilities or Avista Energy engaged in any efforts to manipulate the western energy markets during 2000 and 2001. An agreement in resolution, including these findings, was filed with the FERC's administrative law judge in January 2003. Avista Corp., Avista Energy and the FERC Staff have requested that the administrative law judge certify the agreement in resolution and forward it to the FERC for approval.

Pacific Northwest Refund Proceedings
The July 2001 FERC order also directed an evidentiary proceeding to explore wholesale power market issues in the Pacific Northwest to determine whether there were excessive charges for spot market sales in the Pacific Northwest during the period from December 25, 2000 to June 20, 2001. Based on their application of selected retroactive pricing methods, certain parties asserted claims for significant refunds from Avista Energy and lesser refunds from Avista Utilities. Avista Energy and Avista Utilities joined with numerous other wholesale market participants to oppose proposals by parties for retroactive price caps and refund claims. In September 2001, the FERC's administrative law judge for this proceeding issued a recommendation that the FERC should not order refunds for the Pacific Northwest for the period in question and that the FERC should take no further action on these matters. On December 19, 2002, the FERC issued a Discovery Order that reopened the evidentiary record and allowed parties in the proceeding to conduct additional discovery for the period January 1, 2000 to June 20, 2001. The December 19, 2002 Discovery Order required that, by no later than March 3, 2003, the market participants provide relevant documents to support any proposed recommendations to the FERC. The Discovery Order also affords parties in this proceeding the opportunity to respond by March 20, 2003 to submissions made by March 3, 2003. The Company cannot predict when the FERC will issue a decision in the Pacific Northwest refund proceeding. If retroactive price caps or refunds are imposed, Avista Utilities and Avista Energy could assert offsetting claims in the Pacific Northwest refund proceeding.

See further information under "Federal Energy Regulatory Commission Inquiry," "U.S. Commodity Futures Trading Commission (CFTC) Subpoena," "California Energy Markets" and "Washington Consumer Class Action Lawsuit" in "Note 28 of the Notes to Consolidated Financial Statements."

Regional Transmission Organizations
Avista Corp. is negotiating with nine other utilities in the western United States in the possible formation of a Regional Transmission Organization (RTO), RTO West, a non-profit organization. The potential formation of RTO West is in response to a FERC order requiring all utilities subject to FERC regulation to file a proposal to form a RTO, or a description of efforts to participate in a RTO, and any existing obstacles to RTO participation. RTO West filed its Stage 2 proposal with the FERC in March 2002 and received limited approval from the FERC of this initial plan in September 2002. The FERC's goal with respect to the formation of RTOs is to promote efficiency in wholesale electricity markets and in the operation of transmission systems by way of standardized and independent operation of transmission systems.

Avista Corp. and two other western utilities have also taken steps toward the formation of a for-profit Independent Transmission Company, TransConnect, which would be a member of RTO West, serve portions of five states and own or lease the high voltage transmission facilities of the participating utilities. TransConnect filed its proposal with the FERC in November 2001 and received limited approval from the FERC in September 2002.

The final proposals must be approved by the FERC, the boards of directors of the filing companies and regulators in various states. The companies' decision to move forward with the formation of TransConnect or RTO West will ultimately depend on the conditions related to the formation of the entities, as well as the economics and conditions imposed in the regulatory approval process. If TransConnect were formed, it could result in Avista Utilities divesting its electric transmission assets. The formation of RTO West or TransConnect could have an impact on the Company's transmission costs.

Standard Market Design
On July 31, 2002, the FERC issued a Notice of Proposed Rulemaking proposing a Standard Market Design (SMD) that would significantly alter the markets for wholesale electricity and transmission and ancillary services in the United States. The new SMD would establish a generation adequacy requirement for "load-serving entities" and a standard platform for the sale of electricity and transmission services. Under the new SMD, Independent Transmission Providers would administer spot markets for wholesale power, ancillary services and transmission congestion rights, and electric utilities, including Avista Utilities, would be required to transfer control over transmission facilities to the applicable Independent Transmission Provider. As the SMD proposal develops, the Company continues to assess the impact the SMD would have on its operations as well as how the SMD would impact the RTO West and TransConnect proposals. The Company is subject to state regulation in each of the states in which it operates. State regulatory agencies are actively involved in the SMD rulemaking process and there have been significant concerns at the state and regional level raised with the FERC with respect to the SMD, particularly in the western United States. In February 2003, Avista Utilities and several other western utilities filed comments with the FERC expressing their concerns with respect to the SMD proposal.

Results of Operations

Overall Operations

Diluted earnings (loss) per common share by business segments

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

	2002	2001	2000
Avista Utilities	$0.71	$0.46	$(1.37)
Energy Trading and Marketing	0.47	1.33	3.51
Information and Technology	(0.25)	(0.41)	(0.41)
Other	(0.26)	(0.18)	(0.06)
Earnings per common share from continuing operations	0.67	1.20	1.67
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.20	1.47
Loss per common share from cumulative effect of accounting change	(0.09)	-	-
Total earnings per common share, diluted	$0.60	$0.20	$1.47

2002 compared to 2001

Income from continuing operations was $34.3 million for 2002 compared to $59.6 million for 2001. The decrease was primarily due to reduced net income recorded by the Energy Trading and Marketing line of business. Energy Trading and Marketing recorded net income of $22.4 million for 2002 compared to $63.2 million for 2001. The primary reason for the decrease in net income was a reduction in Avista Energy's net margin. During the second half of 2001 and 2002, prices, trading volumes and volatility in wholesale energy markets in the western United States decreased relative to the first half of 2001, which reduced Avista Energy's earnings potential. Net income recorded by Avista Utilities was $36.4 million for 2002, compared to $24.2 million for 2001. The increase for Avista Utilities is primarily due to an increase in gross margin (operating revenues less resource costs) primarily due to an electric rate increase in Washington, partially offset by an increase in other operating expenses.

The Information and Technology line of business incurred a net loss of $12.1 million for 2002 compared to $19.4 million for 2001. The decrease in the net loss was primarily due to a decrease in operating expenses.

The Other line of business incurred a net loss of $12.4 million for 2002 compared to $8.4 million for 2001. The increase in the net loss was primarily due to litigation costs and settlements.

The discontinued operations of Avista Communications recorded net income of $1.1 million for 2002 compared to a net loss of $47.4 million for 2001. Net income for 2002 was primarily due to the settlement of contracts and liabilities as well as the favorable settlement of a lawsuit. The significant loss for 2001 was primarily due to asset impairment charges of $58.4 million.

Total revenues decreased $414.9 million for 2002 compared to 2001. Avista Utilities' revenues decreased $336.9 million, or 27 percent, primarily due to decreased wholesale electric revenues, partially offset by increased retail electric revenues. Wholesale sales volumes decreased primarily due to the expiration of several wholesale electric sales contracts. The decrease in wholesale revenues also reflected a decrease in wholesale prices. The increase in retail electric revenues was primarily a result of higher rates approved by state regulatory commissions to recover deferred power costs as well as the general electric rate case order approved by the WUTC in June 2002. Revenues from Energy Trading and Marketing decreased $80.1 million, or 60 percent, primarily due to decreased energy commodity prices and trading volumes, as well as reduced market volatility. Revenues from the Information and Technology companies increased 28 percent to $17.6 million primarily as a result of customer growth at Avista Advantage. Revenues from the Other line of business decreased $1.7 million reflecting decreased activity in this line of business.

Total resource costs (all from Avista Utilities) decreased $396.5 million for 2002 compared to 2001 primarily due to reduced power purchase expenses, decreased cost of natural gas purchased to serve retail customers and decreased fuel for generation expenses. Power purchase expenses, natural gas purchased and fuel for generation decreased due to lower wholesale market prices, increased hydroelectric generation, reduced wholesale sales obligations and decreased thermal generation. The net amortization of deferred power and natural gas costs was $68.5 million for 2002, compared to net deferrals of $210.5 million for 2001.

Operations and maintenance expenses decreased $2.7 million primarily due to reduced expenses for Information and Technology. During 2002, Avista Advantage and Avista Labs focused on reducing operating expenses by improving efficiencies and reducing the workforce.

Administrative and general expenses decreased $0.5 million; however, there were significant fluctuations within each business segment. The net decrease was due to reduced expenses for Energy Trading and Marketing as well as Information and Technology, partially offset by increased expenses for Avista Utilities and Other. The decrease for Energy Trading and Marketing was primarily a result of reduced incentive compensation expenses resulting from decreased earnings as well as reduced professional fees. The decrease for Information and Technology was consistent with the decrease in operations and maintenance expenses. The increase for Avista Utilities was primarily due to initiatives implemented during the third quarter of 2001 designed to temporarily reduce certain operating expenses to improve liquidity and operating cash flows. These initiatives resulted in significantly reduced expenses for 2001. Cost reduction measures were not as restrictive during 2002 as the second half of 2001. The increase in administrative and general expenses for Avista Utilities was also due to increased pension, health care, legal and general insurance costs. Administrative and general expenses for the Other business segment increased due to litigation costs and settlements.

Depreciation and amortization increased $1.3 million due to an increase for Avista Utilities partially offset by decreases for each of the other business segments. The decreases for the other business segments were primarily due to the requirement of Statement of Financial Accounting Standards (SFAS) No. 142 "Goodwill and Other Intangible Assets" that goodwill no longer be amortized effective January 1, 2002.

Taxes other than income taxes increased $8.1 million primarily due to increased retail electric revenues and related taxes for Avista Utilities. The increase for Avista Utilities was partially offset by a decrease for Energy Trading and Marketing due to a decrease in the net margin on energy trading activities.

Interest expense decreased $1.1 million for 2002 compared to 2001. The average balance of debt outstanding was relatively consistent for 2001 and 2002 with increasing balances outstanding during 2001 and decreasing balances outstanding during 2002. The amount of debt outstanding increased substantially during 2001 with the issuance of $400.0 million of Unsecured Senior Notes in April 2001 and $150.0 million of First Mortgage Bonds in December 2001. During 2002, the Company repurchased $203.6 million of long-term debt. The Company expects interest expense to continue to decline in 2003 due to the effect of debt repurchases in 2002, expected debt repurchases in 2003 and scheduled debt maturities in 2003.

Capitalized interest decreased $3.0 million for 2002 compared to 2001 primarily due to the fact that the Company did not capitalize any interest related to Coyote Springs 2 subsequent to September 30, 2002 because the project was substantially completed. A decrease in capital expenditures for Avista Utilities also contributed to the decrease in capitalized interest.

Other income-net decreased $3.2 million primarily due to reduced interest income partially offset by impairment charges recorded during 2001.

Income taxes decreased $4.4 million for 2002 compared to 2001, primarily due to decreased earnings before income taxes, partially offset by an increase in state income taxes. The effective tax rate was 46.6 percent for 2002 compared to 36.6 percent for 2001. The increase in the effective tax rate was due to increased state income tax expense as well as decreased earnings and the increased effect of permanent tax differences, such as accelerated tax depreciation, resulting from the Company's previous transition to SFAS No. 109, "Accounting for Income Taxes."

In April 2002, the Company completed its transitional test of goodwill related to the adoption of SFAS No. 142. Accordingly, the Company determined that $6.4 million of goodwill related to Advanced Manufacturing and Development, a subsidiary of Avista Ventures, was impaired. The Company recorded this impairment of $4.1 million, net of tax, as a cumulative effect of accounting change in the Consolidated Statement of Income and Comprehensive Income.

2001 compared to 2000

Income from continuing operations was $59.6 million for 2001 compared to $101.1 million for 2000. The decrease was primarily due to reduced net income recorded by the Energy Trading and Marketing line of business, partially offset by an increase in net income from Avista Utilities. Also contributing to the decline in income from continuing operations was an increase in interest expense and $21.8 million of deferred power costs written off during 2001. The Energy Trading and Marketing line of business recorded net income of $63.2 million in 2001 compared to $161.8 million in 2000. The primary reason for the decrease in net income was a reduction in the mark-to-market adjustment for the change in the fair value position of Avista Energy's energy commodity portfolio. During the second half of 2001, volatility in wholesale energy markets in the western United States decreased, which reduced Avista Energy's earnings potential. Net income recorded by Avista Utilities was $24.2 million in 2001, an increase from a net loss of $38.8 million in 2000. Avista Utilities' net loss for 2000 was primarily due to unprecedented sustained peaks in electric energy prices compounded by a wholesale short position.

The Information and Technology line of business incurred a net loss of $19.4 million for 2001 compared to $19.0 million for 2000 as Avista Advantage and Avista Labs continued to grow their operations.

The Other line of business incurred a net loss of $8.4 million for 2001 compared to $2.9 million for 2000. The increase in the net loss from 2000 was primarily a result of increased interest expense on intercompany borrowings between Avista Capital and Avista Corp. that is eliminated in the consolidated financial statements.

The discontinued operations of Avista Communications incurred a net loss of $47.4 million for 2001 compared to a net loss of $9.4 million for 2000. The significant loss from Avista Communications was primarily due to pre-tax asset impairment charges of $58.4 million recorded during the third quarter of 2001.

Total revenues decreased $463.2 million in 2001 compared to 2000. Avista Utilities' revenues decreased $281.3 million, or 19 percent, primarily due to decreased wholesale electric sales partially offset by increased retail revenues from both electric and natural gas sales. The increase in retail revenues is primarily a result of higher rates approved by state regulatory agencies to recover deferred power and natural gas costs. Revenues from the Energy Trading and Marketing line of business decreased $173.5 million, or 56 percent, due to a decrease in unrealized gains. Revenues from the Information and Technology companies increased 141 percent to $13.8 million primarily as a result of customer growth at Avista Advantage. Revenues from the Other line of business decreased $16.6 million, or 50 percent, reflecting decreased activity in this line of business.

Avista Utilities' resource costs decreased $396.5 million in 2001 compared to 2000, or 32 percent, primarily due to reduced wholesale power purchases.

Administrative and general expenses decreased $15.7 million in 2001 compared to 2000 primarily due to reduced expenses for Avista Utilities and Energy Trading and Marketing. This was primarily a result of company-wide initiatives to reduce expenses. This was also due to decreased incentive compensation expense based on lower earnings by both Avista Energy and the Company.

Interest expense increased $38.2 million in 2001 compared to 2000, primarily due to higher levels of outstanding debt during the year. Long-term debt and short-term borrowings outstanding as of December 31, 2001 increased $320.2 million from December 31, 2000.

Capitalized interest increased $7.1 million from 2000 to 2001 primarily due to increased capitalized interest for Coyote Springs 2.

Income taxes decreased $42.6 million in 2001 compared to 2000, primarily due to decreased earnings before income taxes. The effective tax rate was 36.6 percent for 2001 compared to 43.2 percent for 2000. The higher effective tax rate in 2000 was primarily due to higher state income taxes.

Preferred stock dividend requirements decreased from 2000 due to the conversion of all outstanding shares of Series L Preferred Stock into shares of common stock, which resulted in a one-time charge of $21.3 million for preferred stock dividend requirements in 2000.

Avista Utilities

2002 compared to 2001

Avista Utilities recorded net income of $36.4 million for 2002 compared to $24.2 million for 2001. Avista Utilities' income from operations was $149.2 million for 2002 compared to $114.9 million for 2001. This increase was primarily due to an increase in gross margin (operating revenues less resource costs). Avista Utilities' operating revenues decreased $336.9 million and resource costs decreased $396.5 million resulting in an increase of $59.6 million in gross margin for 2002 as compared to 2001. The increase in gross margin was partially offset by an increase in administrative and general expenses, depreciation and amortization and taxes other than income taxes. The general electric rate increase of 19.3 percent in Washington base retail rates effective July 1, 2002 contributed to the increase in gross margin.

Retail electric revenues increased $65.2 million for 2002 from 2001. This increase was primarily due to the electric surcharges implemented to recover deferred power costs and the June 2002 Washington electric rate increase, partially offset by decreased use per customer and total kWhs sold. The increase in retail electric revenues was also due to refunds to customers in January 2001 of the gain on the sale of Avista Utilities' interest in the Centralia Power Plant (Centralia) that reduced revenues for 2001. During 2001 and 2002, Avista Utilities experienced decreased loads and decreased use per customer with respect to electric retail sales. The decrease in use per customer appears to be primarily due to a response to the increase in electric rates and the resulting conservation efforts of individual customers. The decrease in use per customer also appears to reflect milder weather in 2002 and 2001 as compared to 2000. The decrease in total kWhs sold primarily relates to industrial customers and appears to reflect a general downturn in the economy of eastern Washington and northern Idaho.

Wholesale electric revenues decreased $416.8 million, or 87 percent, reflecting wholesale sales volumes which decreased 65 percent from 2001 and average sales prices that were 62 percent lower than the prior year. Average wholesale prices decreased to $28.92 per MWh for 2002 from $76.80 per MWh for 2001 reflecting decreased electric prices in the western United States. Wholesale sales volumes decreased primarily due to the expiration of several wholesale electric sales contracts, including two 100 MW index-based sales contracts that expired in July 2001. The extent of future wholesale transactions will be based on the availability of resources owned or controlled by Avista Utilities and changes to loads of Avista Utilities' customers and contractual obligations.

Other electric revenues increased $13.5 million primarily due to the sale of natural gas purchased for electric generation that was not used in generation. Avista Utilities operated less thermal generation in 2002 as compared to 2001 based on lower retail demand, increased hydroelectric generation and decreased wholesale market prices.

Natural gas revenues increased $1.2 million for 2002 from 2001 due to a slight increase in retail and transportation revenues, partially offset by a decrease in wholesale natural gas revenues. Retail rates were increased during 2001 to recover deferred natural gas costs. During the fourth quarter of 2002, retail rates for natural gas were reduced in response to a decrease in current and projected natural gas costs. During 2001 and 2002, Avista Utilities experienced decreased loads and decreased use per customer with respect to natural gas retail sales. The decrease in use per customer appears to be primarily due to a response to the increase in natural gas rates during 2001 and the resulting conservation efforts of individual customers. The decrease in use per customer also appears to reflect milder weather in 2002 and 2001 as compared to 2000. The decrease in total therms sold primarily relates to industrial customers and appears to reflect a general downturn in the economy of Avista Utilities' service territory.

Power purchased for 2002 decreased $593.0 million, or 84 percent, compared to 2001 due to the decreased volume and price of power purchases. Average purchased power prices for 2002 were $24.64 per MWh or 68 percent lower than $77.40 per MWh for 2001 and volumes purchased decreased 49 percent compared to 2001. The decrease in the volume of purchased power was primarily the result of decreases in the volume of wholesale electric sales and increased hydroelectric resource availability to meet retail demand.

Net amortization of deferred power costs was $26.3 million in 2002 compared to net deferrals of $202.8 million in 2001. During 2002, Avista Utilities recovered (collected as revenue) $38.6 million of previously deferred power costs in Washington and $24.7 million in Idaho. During 2002, Avista Utilities deferred $22.4 million of power costs in Washington and $13.5 million in Idaho. During 2002, $27.7 million of a deferred credit was offset against the Idaho share of deferred power costs. The deferred credit relates to funds received in December 1998 in which the Company assigned and transferred certain rights under a long-term power sales contract with Portland General Electric (PGE) to a funding trust. Total deferred power costs were $155.3 million as of December 31, 2002. See further description of issues related to deferred power costs in the section "Avista Utilities – Regulatory Matters."

During 2002, Avista Utilities had $42.2 million of net amortization of deferred natural gas costs compared to net deferrals of $7.7 million in 2001. Total deferred natural gas costs were $11.5 million as of December 31, 2002.

The cost of fuel for generation for 2002 decreased $63.4 million from 2001 primarily due to a decrease in thermal generation as well as a decrease in the average cost of natural gas used for generation. Thermal generation decreased 43 percent primarily due to increased hydroelectric generation and wholesale market prices that were generally below the cost of operating the thermal generating units.

The expense for natural gas purchased for 2002 decreased $50.0 million compared to 2001 primarily due to the decreased average cost of natural gas.

Other fuel costs for 2002 increased $34.6 million compared to 2001. This was due to an increase in natural gas purchased as fuel for electric generation that was not used. This excess natural gas was sold with the associated revenues reflected as other electric revenues. Other fuel costs exceeded the revenues from selling the excess natural gas. This excess cost is accounted for under the ERM in Washington and the PCA in Idaho.

2001 compared to 2000

Avista Utilities recorded net income of $24.2 million in 2001 compared to a net loss of $38.8 million in 2000. Avista Utilities' income from operations was $114.9 million for 2001 compared to $3.2 million for 2000. This increase was primarily due to an increase in gross margin (operating revenues less resource costs). Avista Utilities' operating revenues decreased $281 million and resource costs decreased $396 million resulting in an increase of $115 million in gross margin for 2001 as compared to 2000.

Based on views of streamflows, historic wholesale market prices and energy availability in the second quarter of 2000, Avista Utilities entered into contracts and sold call options for fixed-price power for delivery without making matching purchases at the same time. Avista Utilities also made certain short-term sales at fixed prices that were offset by purchases at prices indexed to the market price at the time of delivery. Certain of these wholesale trading positions were outside normal operating guidelines. Avista Utilities was required to buy additional power not only to meet its obligations to its retail and long-term wholesale customers, but also to cover its wholesale trading positions. An orderly process to complete the necessary power purchases was impeded by the rapid escalation of market prices and lack of liquidity in the power markets during the second quarter of 2000. These purchases were made at fixed prices significantly higher than the related selling prices and at index, which settled at unprecedented levels in June 2000. The pricing of these purchases caused the majority of Avista Utilities' net loss for 2000.

Avista Utilities' short position was compounded by the May 2000 sale of its interest in Centralia to TransAlta, which reduced its system capacity by 200 megawatts. Based on historical trends and Avista Utilities' views on power prices and availability of power for May and June 2000, Avista Utilities did not seek to replace Centralia generation for those two months with firm commitments. Avista Utilities entered into a three-and-one-half-year contract to purchase 200 megawatts from TransAlta beginning in July 2000.

Retail electric revenues increased $4.0 million for 2001 from 2000. This increase was primarily due to the electric surcharges implemented in Washington and Idaho to recover deferred power costs, partially offset by decreased use per customer and kWh sold. Wholesale electric revenues decreased $383.9 million, or 44 percent, while wholesale sales volumes decreased 60 percent from 2000, reflecting average sales prices that were 40 percent higher than the prior year. Wholesale sales volumes decreased due to management's decision in 2000 to reduce power imbalance volume limits (the difference between projected load obligations and projected resource availability). This decision was based on the emergent market price volatility, and Avista Utilities' strategy to focus primarily on energy transactions necessary to efficiently manage power resources to meet retail customer loads and wholesale obligations.

Natural gas revenues increased $83.8 million for 2001 from 2000 due to increased prices approved by state commissions to recover increased natural gas costs partially offset by decreased therm sales, primarily due to both decreased retail and transportation customer volumes.

Power purchased during 2001 decreased $364.2 million, or 34 percent compared to 2000 primarily due to the decreased volume of power purchases, partially offset by higher average prices. Average purchased power prices for 2001 were 28 percent higher than for 2000; however, volumes purchased decreased 48 percent. The decrease in the volume of purchased power was primarily the result of decreases in the volume of wholesale electric sales.

During 2001 Avista Utilities deferred $145.4 million (net of the $21.8 million write-off) in power costs in Washington and $73.7 million in Idaho. The total balance of deferred power costs was $140.2 million for Washington and $73.1 million for Idaho as of December 31, 2001. In September 2001, the WUTC approved a temporary electric surcharge of 25 percent. In 2001, revenue collected under the Washington surcharge was $10.2 million, and $53.8 million of a deferred credit on the Company's balance sheet relating to funds received from a power sales contract with PGE in 1998 was offset against deferred power costs. In October 2001, the IPUC approved a PCA surcharge and the extension of a previously approved PCA surcharge for a total of 19.4 percent. In 2001, revenue collected under the Idaho PCA surcharges was $6.1 million, and $6.9 million of a deferred credit on the Company's balance sheet relating to funds received from a power sales contract with PGE in 1998 was offset against deferred power costs. In March 2002, the WUTC issued an order approving the prudence and recoverability of 90 percent of deferred power supply costs incurred during the period from July 1, 2000 through December 31, 2001. This resulted in the Company recording an additional expense for $21.8 million (representing the 10 percent of costs not recoverable) of power supply costs previously deferred through 2001. Additionally, the order also provided that one-fifth of the 25 percent electric surcharge will be applied to offset the Company's general operating costs and the remainder will continue to be applied as a recovery of deferred power costs. The WUTC order also approved a 6.2 percent (or $14.7 million in annual revenues) increase in base retail rates. See further description of issues related to deferred power costs in the section "Avista Utilities – Regulatory Matters."

Avista Utilities deferred, net of amortization, $7.7 million of purchased natural gas costs during 2001 and total deferred natural gas costs were $52.7 million as of December 31, 2001. In July 2001, the Company filed requests for purchased gas cost adjustments (PGA) with the WUTC and the IPUC in order to recover certain deferred natural gas costs related to Washington and Idaho natural gas purchases. The Washington PGA increase of 12.2 percent approved by the WUTC and the Idaho PGA increase of 11.5 percent approved by the IPUC became effective in August 2001.

The cost of fuel for generation for 2001 increased $12.9 million from 2000 primarily due to an increase in natural gas-fired combustion turbine plant generation and partially due to the increased cost of natural gas. Natural gas costs were relatively high compared to historical prices during the first half of 2001 before declining in the second half of 2001.

The expense for natural gas purchased for resale for 2001 increased $50.8 million compared to 2000 due to the increased cost of natural gas partially offset by a decrease in total therms sold. Consistent with changes in fuel for generation, natural gas costs declined during the second half of 2001 as compared to the first half of the year.

As part of the strategy to mitigate the decline in electric resources caused by poor hydroelectric conditions and volatile energy markets, Avista Utilities had several buy-back and rebate programs for residential, commercial and industrial customers during 2001. The programs were designed to encourage conservation and decrease average customer usage.

Energy Trading and Marketing

Energy Trading and Marketing includes the results of Avista Energy and Avista Power.

Avista Energy is an electricity and natural gas marketing and trading business, operating primarily within the WECC. Avista Energy focuses on asset-backed optimization of combustion turbines and hydroelectric assets owned by other entities, long-term electric supply contracts, natural gas storage, and electric and natural gas transmission and transportation arrangements. Avista Energy's marketing efforts are driven by its base of knowledge and experience in the operation of both electric energy and natural gas physical systems in the WECC, as well as its relationship-focused approach with its customers.

In June 2002, the Emerging Issues Task Force (EITF) reached a partial consensus on Issue No. 02-3 regarding the accounting for contracts involved in energy trading and risk management activities. The partial consensus required that all gains and losses arising from energy trading contracts (whether realized or unrealized) accounted for under EITF Issue No. 98-10 "Accounting for Contracts Involved in Energy Trading and Risk Management Activities" were to be presented on a net basis in the income statement beginning in the third quarter of 2002. Reclassification of all historical comparable periods was required. Avista Energy historically presented unrealized gains and losses on energy trading contracts on a net basis. However, realized contracts were presented on a gross basis for both operating revenues and resource costs. The implementation of EITF Issue 02-3 resulted in reduced operating revenues and resource costs as compared to historical periods with no impact on the Company's net income or financial condition.

Avista Energy accounted for energy commodity trading activity in compliance with EITF Issue No. 98-10 through December 31, 2002 for contracts entered into on or prior to October 25, 2002. Under EITF 98-10, Avista Energy recognized revenue based on the change in the market value of outstanding derivative commodity sales contracts, net of future servicing costs and reserves, in addition to revenue related to settled contracts. In October 2002, the EITF rescinded Issue No. 98-10. As such, Avista Energy is required to account for energy trading contracts that meet the definition of a derivative at market value in compliance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." This applies to all existing contracts as of January 1, 2003 as well as to all new contracts entered into subsequent to October 25, 2002. Contracts not meeting the definition of a derivative are no longer accounted for at market value and include Avista Energy's Agency Agreement with Avista Utilities, natural gas storage contracts, tolling agreements and natural gas transportation agreements. The transition from EITF Issue No. 98-10 to accrual based accounting resulted in the adjustment of the contracts that are not considered derivatives from their market value to their cost basis. Any gain or loss on contracts that are not considered derivatives will not be recognized until the contract is settled or realized. The Company anticipates that the changes will primarily affect the timing of the recognition of income or loss in earnings, and not change the underlying economics or cash flows of transactions entered into by Avista Energy. The changes could result in a significant increase in the volatility of reported earnings on a quarter-to-quarter and year-to-year basis. On January 1, 2003, Avista Energy recorded as a cumulative effect of accounting change a charge of approximately $1.2 million (net of tax) related to the transition from EITF 98-10 to SFAS No. 133. See "Critical Accounting Policies" and "Note 2 of the Notes to Consolidated Financial Statements" for further details.

Derivative commodity instruments in the energy trading portfolio are marked to estimated fair market value on a daily basis (mark-to-market accounting), which causes earnings variability. Market prices are utilized in determining the value of electric, natural gas and related derivative commodity instruments. For natural gas commodity instruments, these market prices are generally available through three years. For electric commodity instruments, these market prices are generally available through two years. For longer-term positions and certain short-term positions for which market prices are not available, models based on forward price curves are utilized. These models incorporate a variety of estimates and assumptions, the ultimate outcomes of which are beyond Avista Energy's control including, among others, estimates and assumptions as to demand growth, fuel price escalation, availability of existing generation and costs of new generation. Actual experience can vary significantly from these estimates and assumptions.

Avista Energy trades electricity and natural gas, along with derivative commodity instruments including futures, options, swaps and other contractual arrangements. Most transactions are conducted on a largely unregulated "over-the-counter" basis, there being no central clearing mechanism (except in the case of specific instruments traded on the commodity exchanges). Avista Energy's trading operations are affected by, among other things, volatility of prices within the electric energy and natural gas markets, the demand for and availability of energy, lower unit margins on new sales contracts, FERC-ordered price caps, deregulation of the electric utility industry, the creditworthiness of counterparties and the reduced liquidity in energy markets. See "Business Risk" for further information.

2002 compared to 2001

Energy Trading and Marketing's net income was $22.4 million for 2002, compared to $63.2 million for 2001. The primary reason for the decrease in net income was a decrease in the net margin on energy trading activities. Net margin on energy trading activities, which is reported as operating revenues, was $54.2 million for 2002 compared to $134.3 million for 2001.

Realized gains decreased to $141.6 million for 2002 from $164.5 million for 2001. Realized gains represent the net gain on contracts that have settled. The decrease was primarily due to a decrease in the underlying commodity values that settled and a decrease in the volume of transactions. The decrease in the volume of transactions was primarily due to reduced liquidity in wholesale markets, fewer creditworthy counterparties participating in the wholesale markets and a decrease in the volatility of prices in the wholesale markets. The total mark-to-market adjustment for Energy Trading and Marketing was an unrealized loss of $87.4 million for 2002 compared to an unrealized loss of $30.2 million for 2001. The increase in the unrealized loss is primarily due to the settlement of contracts and the realization of previously unrealized gains and decreased volatility in the wholesale energy markets. During 2002, the change in the total unrealized gain attributable to market prices and other market changes was $49.7 million, a decrease from $120.6 million in 2001.

Administrative and general expenses decreased $11.7 million, or 35 percent, from 2001 primarily due to reduced incentive compensation expense based on lower earnings in 2002. Reduced professional fees also contributed to the decrease in administrative and general expenses. Professional fees were high during 2001 due to expenses associated with the California energy crisis (see "Power Market Issues") and a CFTC investigation that was resolved in 2001 related to certain trades in 1998.

Energy Trading and Marketing's total assets decreased $156.6 million from December 31, 2001 to December 31, 2002 primarily due to a decrease in total current and non-current energy commodity assets. This decrease in commodity assets reflects the settlement of contracts and a decrease in commodity prices during 2002.

2001 compared to 2000

Energy Trading and Marketing's net income was $63.2 million for 2001, compared to $161.8 million for 2000. The primary reason for the decrease in net income was a decrease in the mark-to-market adjustment for the change in the fair value position of Avista Energy's energy commodity portfolio. The mark-to-market adjustment was an unrealized loss of $30.2 million for 2001 compared to an unrealized gain of $176.8 million for 2000. The decrease is primarily due to a significant amount of contracts settled during 2001 and the realization of previous unrealized gains. Volatility in energy markets and increased commodity prices during 2000 resulted in significant unrealized gains during 2000. These unrealized gains were partially realized during 2001. Realized gains increased to $164.5 million in 2001 from $130.9 million in 2000.

Administrative and general expenses decreased $7.8 million or 19 percent from 2000 primarily due to reduced incentive compensation expense based on lower earnings in 2001.

Expenses associated with the exit of Avista Energy's operations in Houston and Boston during the first half of 2000 totaled $7.9 million in 2000.

During 2001 the Company recorded an impairment charge of $8.2 million related to three turbines owned by Avista Power which is reflected in the line item other income-net in the Consolidated Statements of Income and Comprehensive Income. The Company originally planned to use these turbines in a non-regulated generation project. During 2001, the Company decided that it would no longer pursue the development of additional non-regulated generation projects. As such, the Company wrote down the carrying value of the turbines to estimated fair value less selling costs.

Energy Trading and Marketing's total assets decreased $8.8 billion from December 31, 2000 to December 31, 2001 primarily due to a decrease in total current and non-current energy commodity assets. This decrease in commodity assets primarily reflected the settlement of a significant amount of contracts during 2001 and a decrease in the forward price and estimated value of natural gas and electricity from December 31, 2000 to December 31, 2001.

Energy trading activities and positions

The following summarizes information with respect to Avista Energy's trading activities during 2002 (dollars in thousands):

	Natural Gas Assets net of Liabilities	Electric Assets net of Liabilities	Total Unrealized Gain (Loss) (4)
Fair value of contracts as of December 31, 2001	$38,392	$148,325	$186,717
Less contracts settled during 2002 (1)	(33,334)	(108,276)	(141,610)
Fair value of new contracts when entered into during 2002 (2)	-	-	-
Change in fair value due to changes in valuation techniques (3)	-	-	-
Change in fair value attributable to market prices and other market changes	29,662	20,032	49,694
Fair value of contracts as of December 31, 2002	$34,720	$60,081	$94,801

(1) Contracts settled during 2002 include those contracts that were open in 2001 but settled during 2002 as well as new contracts entered into and settled during 2002. Amount represents realized gains associated with these settled transactions.
(2) Avista Energy has not entered into any origination transactions during 2002 in which dealer profit or mark-to-market gain or loss was recorded at inception.
(3) During 2002, Avista Energy did not experience a change in fair value as a result of changes in valuation techniques.
(4) Change in unrealized gain (loss) does not reconcile to totals for the Energy Trading and Marketing segment due to an intercompany elimination between Avista Energy and Avista Power related to Avista Energy's contract for the output from the Lancaster Project that is 49 percent owned by Avista Power.

The following discloses summarized information with respect to valuation techniques and contractual maturities of Avista Energy's energy commodity contracts outstanding as of December 31, 2002 (dollars in thousands):

	Less than one year	Greater than one and less than three years	Greater than three and less than five years	Greater than five years	Total
Natural gas assets (liabilities), net (1)					
Prices from other external sources (2)	$25,622	$ 2,144	$ -	$ -	$27,766
Fair value based on valuation models (3)	6,345	(1,351)	1,184	776	6,954
Total natural gas assets (liabilities), net	$31,967	$ 793	$1,184	$ 776	$34,720
Electric assets (liabilities), net (1)					
Prices from other external sources (2)	$30,659	$21,688	$ -	$ -	$52,347
Fair value based on valuation models (4)	(1,929)	5,415	9,304	(5,056)	7,734
Total electric assets (liabilities), net	$28,730	$27,103	$9,304	$(5,056)	$60,081

(1) Reflects commodity contracts outstanding and accounted for under EITF 98-10 as of December 31, 2002 with the exception of contracts entered into subsequent to October 25, 2002. The table does not reflect any adjustment for the transition to SFAS No. 133 for contracts not meeting the definition of a derivative. Effective January 1, 2003, contracts that were entered into on or prior to October 25, 2002 and not meeting the definition of a derivative are accounted for on an accrual basis. Contracts not meeting the definition of a derivative include Avista Energy's Agency Agreement with Avista Utilities, natural gas storage contracts, tolling agreements and natural gas transportation agreements.
(2) Fair value is determined based upon actively traded, "over-the-counter" market quotes received from third party brokers. For natural gas assets and liabilities, these market quotes are generally available through three years. For electric assets and liabilities, these market quotes are generally available through two years.
(3) Represents contracts for delivery at basis locations not actively traded in the "over-the-counter" markets. In addition, this includes all contracts with a delivery period greater than three years, for which active quotes are not available. These internally developed market curves are based upon published New York Mercantile Exchange prices through seven years, as well as basis spreads using historical and broker estimates. After seven years, an escalation is used to estimate the valuation.
(4) Represents contracts for delivery at basis locations not actively traded in the "over-the-counter" markets. In addition, this includes all contracts with a delivery period greater than two years, for which active quotes are not available. These internally developed market curves are determined using a production cost model with

inputs for assumptions related to power prices (including, without limitation, natural gas prices, generation on line, transmission constraints, future demand and weather).

Avista Energy conducts frequent stress tests on the valuation of its portfolio. By changing the input assumptions to the internally developed market curves, these stress tests attempt to capture Avista Energy's sensitivity to changes in portfolio valuation. These stress tests indicate that, for the portfolio valued under internally developed market curves, the valuations can be reasonably certain to be within a 20 percent range, upwards or downwards, of the reported values listed above.

Avista Power

Avista Power is a 49 percent owner of a 270 MW natural gas-fired combustion turbine plant in northern Idaho (Lancaster Project), which commenced commercial operation in September 2001. All of the output from the Lancaster Project is contracted to Avista Energy for 25 years. In addition, Avista Power and its co-owner, an affiliate of Mirant Americas Development, Inc. (Mirant), have substantially completed the construction of Coyote Springs 2. In January 2003, Avista Power's 50 percent ownership interest in Coyote Springs 2 was transferred to Avista Corp. for inclusion in Avista Utilities' power generation resource portfolio. See "New Generation Resource – Avista Utilities" for further information.

Information and Technology

The Information and Technology line of business includes the results of Avista Advantage and Avista Labs (including its 70 percent equity interest in H2fuel, LLC). Avista Advantage remains focused on growing revenue, improving margins, reducing fixed and variable costs and improving client satisfaction. Avista Corp. continues discussions with selected companies in its search for a financial partner for Avista Labs with the goal of reducing its ownership interest in Avista Labs to less than 20 percent.

2002 compared to 2001

Information and Technology's net loss was $12.1 million for 2002 compared to $19.4 million for 2001. Operating revenues for this line of business increased $3.8 million and operating expenses decreased $7.2 million, as compared to 2001. Avista Advantage accounted for the increase in revenues primarily due to the expansion of its customer base. The decrease in operating expenses reflects reduced expenses for Avista Advantage and Avista Labs due to improved efficiencies, a reduction in the number of employees and a focus on reducing operating expenses. Certain non-recurring items in both periods also contributed to the decrease in operating expenses.

2001 compared to 2000

Information and Technology's net loss was $19.4 million for 2001 compared to $19.0 million for 2000. Operating revenues and expenses in 2001 for this line of business increased $8.1 million and $11.5 million, respectively, as compared to 2000. Avista Advantage accounted for the increase in revenues primarily due to the expansion of its customer base. The increase in operating expenses reflected expansion of operations for Avista Advantage and further fuel cell development by Avista Labs.

Other

The Other line of business includes several subsidiaries, including Avista Ventures, Pentzer, Avista Development and Avista Services. The operations of Avista Capital that are not included through its subsidiaries are reported in this line of business.

2002 compared to 2001

The net loss before cumulative effect of accounting change from this line of business was $12.4 million for 2002, compared to $8.4 million for 2001. The increase in the net loss was primarily due to a decrease in income from operations and partially due to an increase in interest expense as well as a reduction in gains on the disposition of assets. Operating revenues from this line of business decreased $1.7 million and operating expenses increased $2.7 million, respectively, for 2002 as compared to 2001. The decrease in income from operations was primarily due to an increase in litigation costs and settlements as well as an increase in the loss from Advanced Manufacturing and Development, a subsidiary of Avista Ventures, from $4.5 million in 2001 to $5.1 million in 2002.

2001 compared to 2000

The net loss from this line of business was $8.4 million for 2001, compared to $2.9 million for 2000. The increase in the net loss from 2000 was primarily a result of increased interest expense on intercompany borrowings between Avista Capital and Avista Corp. that is eliminated in the consolidated financial statements. Operating revenues and expenses from this line of business decreased $16.6 million and $16.0 million, respectively, during 2001 as compared to 2000, reflecting reduced activities in this line of business.

Discontinued Operations

In September 2001, the Company reached a decision that it would dispose of substantially all of the assets of Avista Communications. The divestiture of operating assets was complete by the end of 2002. Certain liabilities of the operations remain to be settled. In October 2001, minority shareholders of Avista Communications acquired ownership of its Montana and Wyoming operations as well as its dial-up internet access operations in Spokane, Washington and Coeur d'Alene, Idaho. In December 2001, Avista Communications completed the sale of the assets and customer accounts of its Yakima and Bellingham, Washington operations to Advanced Telcom Group, Inc. In April 2002, Avista Communications completed the transfer of voice and integrated services customer accounts in Spokane, Washington and Lewiston and Coeur d'Alene, Idaho to certain subsidiaries of XO Communications, Inc. In December 2002, the Company completed the sale of substantially all of the remaining assets of Avista Communications to FiberLink LLC.

2002 compared to 2001

Net income for 2002 was $1.1 million, compared to a net loss of $47.4 million for 2001. Net income for 2002 was primarily due to the settlement of contracts and liabilities during the period as well as the favorable settlement of a lawsuit during the period. The significant net loss for 2001 was due to asset impairment charges of $58.4 million recorded during the third quarter of 2001.

2001 compared to 2000

The net loss for 2001 was $47.4 million, compared to a net loss of $9.4 million for 2000. The significant net loss for 2001 was due to asset impairment charges. The loss from operations for Avista Communications was $21.1 million for 2001 compared to $15.4 million for 2000.

Earnings Outlook

The Company expects to report consolidated earnings in the range of $0.80 to $1.00 per diluted share in 2003. This expectation is for earnings before the cumulative effect of changes in accounting principles. This estimate includes earnings ranging from $0.60 to $0.80 for Avista Utilities and $0.20 to $0.30 for Energy Trading and Marketing and a loss ranging from $0.10 to $0.15 for Information and Technology. The 2003 projection includes uncertainties surrounding reduced activity in the wholesale energy markets and increased expenses, such as pension, health care and insurance costs. The projection for 2003 anticipates that the Company will expense the first $9 million plus 10 percent of any additional power supply costs above the amount allowed in base retail electric rates for Washington customers. The Company anticipates that the change in accounting for Avista Energy's energy trading activities from EITF Issue No. 98-10 to SFAS No. 133 could result in a significant increase in the volatility of reported earnings on a quarter-to-quarter and year-to-year basis. These projections are subject to a variety of risks and uncertainties that could cause actual results to differ from this estimate, including those described above and listed under "Safe Harbor for Forward-Looking Statements" and "Future Outlook-Business Risks." See "Liquidity and Capital Resources" for additional information.

New Generation Resource – Avista Utilities

Construction has been substantially completed on the 280 MW combined cycle natural gas-fired turbine power plant at Coyote Springs 2 located near Boardman, Oregon which was 50 percent owned by Avista Power and 50 percent owned by Mirant and was included in the Energy Trading and Marketing line of business as of December 31, 2002. The Company's ownership interest in the plant was transferred from Avista Power to Avista Corp. in January 2003 to be operated as an asset of Avista Utilities. Avista Corp. and Mirant are both current with respect to their obligations to share equally in the costs of construction of the plant. Avista Corp. and Mirant will share equally in the costs of operation and output from Coyote Springs 2. In May 2002, a transformer at the site failed and caught fire resulting in the release of an estimated 17,000 gallons of coolant oil. The Company worked closely with the appropriate environmental agencies to complete a satisfactory cleanup of the oil. While the cause of the failure is still being investigated, the Company anticipates the cost of the cleanup as well as the cost of replacing the damaged transformer will be considered covered losses under the relevant insurance policies. Additionally, the Company continues to evaluate the merits of possible claims against those parties that may be responsible for the transformer failure. In December 2002, the replacement transformer was received in a damaged condition. The problems with the transformer have delayed the scheduled completion of the project from the third quarter of 2002 to the middle of 2003. As of December 31, 2002, the Company had invested $109.0 million in Coyote Springs 2, including capitalized interest.

New Accounting Standards

See "Note 2 of the Notes to Consolidated Financial Statements."

Critical Accounting Policies

Use of estimates
The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the consolidated financial statements and thus actual results could differ from the amounts reported and disclosed herein.

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

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

The Company's primary regulatory assets include power and natural gas deferrals, investment in exchange power, regulatory assets for deferred income taxes, unamortized debt expense, regulatory asset offsetting energy commodity derivative liabilities (see "Utility Energy Commodity Derivative Assets and Liabilities" for further information), demand side management programs, conservation programs and the provision for postretirement benefits. Deferred credits include regulatory liabilities created when Centralia was sold and the gain on the general office building sale/leaseback, which is being amortized over the life of the lease.

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

Avista Utilities enters into forward contracts to purchase or sell energy. Under forward contracts, Avista Utilities commits to purchase or sell a specified amount of energy at a specified time, or during a specified period, in the future. Certain of these forward contracts are considered derivative instruments. Avista Utilities also records derivative commodity assets and liabilities for over-the-counter and exchange-traded derivative instruments as well as certain long-term contracts. In conjunction with the issuance of SFAS No. 133, the WUTC and the IPUC issued accounting orders requiring Avista Utilities to offset any derivative assets or liabilities with a regulatory asset or liability. This accounting treatment is intended to defer the recognition of mark-to-market gains and losses on energy commodity transactions until the period of settlement. The order provides for Avista Utilities to not recognize the unrealized gain or loss on utility derivative commodity instruments in the Consolidated Statements of Income and Comprehensive Income. Such realized gains or losses are recognized in the period of settlement subject to current or future recovery in retail rates.

Avista Utilities believes that substantially all of its purchases and sales contracts for both capacity and energy qualify as normal purchases and sales under SFAS No. 133 and are not required to be recorded as derivative commodity assets and liabilities. Contracts that are not considered derivatives under SFAS No. 133 are generally accounted for at cost until they are settled unless there is a decline in the fair value of the contract that is determined to be other than temporary.

Interpretations that may be issued by the Derivatives Implementation Group, a task force created to assist the Financial Accounting Standards Board (FASB) in answering questions that companies have in implementing SFAS No. 133, may change the conclusions that the Company has reached regarding accounting for energy contracts. As a result, the accounting treatment and financial statement impact could change in future periods.

Avista Energy Trading Activities

Avista Energy accounted for energy commodity trading activity in compliance with EITF Issue No. 98-10 through December 31, 2002 for contracts entered into on or prior to October 25, 2002. Under EITF 98-10, Avista Energy recognized revenue based on the change in the market value of outstanding derivative commodity sales contracts, net of future servicing costs and reserves, in addition to revenue related to settled contracts. In October 2002, the EITF rescinded Issue No. 98-10. As such, Avista Energy is required to account for energy trading contracts that meet the definition of a derivative at market value in compliance with SFAS No. 133. This applies to all existing contracts as of January 1, 2003 as well as to all new contracts entered into subsequent to October 25, 2002. Contracts not meeting the definition of a derivative are no longer accounted for at market value and include Avista Energy's Agency Agreement with Avista Utilities, natural gas storage contracts, tolling agreements and natural gas transportation agreements. The transition from EITF Issue No. 98-10 to accrual based accounting resulted in the adjustment of the contracts that are not considered derivatives from their market value to their cost basis. Any gain or loss on contracts that are not considered derivatives will not be recognized until the contract is settled or realized. The Company anticipates that the changes will primarily affect the timing of the recognition of income or loss in earnings, and not change the underlying economics or cash flows of transactions entered into by Avista Energy. The changes could result in a significant increase in the volatility of reported earnings on a quarter-to-quarter and year-to-year basis. On January 1, 2003, Avista Energy recorded as a cumulative effect of accounting change a charge of approximately $1.2 million (net of tax) related to the transition from EITF 98-10 to SFAS No. 133.

Market prices are utilized in determining the value of the electric, natural gas and related derivative commodity instruments. For natural gas commodity instruments, these market prices are generally available through three years. For electric commodity instruments, these market prices are generally available through two years. For longer-term positions and certain short-term positions for which market prices are not available, a model to estimate forward price curves is utilized. These models incorporate a variety of estimates and assumptions, the ultimate outcomes of which are beyond Avista Energy's control including, among others, estimates and assumptions as to demand growth, fuel price escalation, availability of existing generation and costs of new generation. Actual experience can vary significantly from these estimates and assumptions. Gains and losses on electric, natural gas and related derivative commodity instruments utilized for trading are recognized as income on a current basis (the mark-to-market method) and are included in the Consolidated Statements of Income and Comprehensive Income in operating revenues on a net basis, and in the Consolidated Balance Sheets as current or non-current energy commodity assets or liabilities. Contracts in a receivable position, as well as the options held, are reported as assets. Similarly, contracts in a payable position, as well as options written, are reported as liabilities. Net cash flows are recognized in the period of settlement.

Pension Plans and Other Postretirement Benefit Plans

The Company has a defined benefit pension plan covering substantially all of its regular full-time employees. Certain of the Company's subsidiaries also participate in this plan. Individual benefits under this plan are based upon years of service and the employee's average compensation as specified in the plan. The Company's funding policy is to contribute amounts that are not less than the minimum amounts required to be funded under the Employee Retirement Income Security Act, nor more than the maximum amounts which are currently deductible for income tax purposes. The Company made $12 million in cash contributions to the pension plan in 2002 and did not make any cash contributions to the pension plan in 2001. The Company expects to contribute approximately $12 million to the pension plan in 2003. Pension fund assets are invested primarily in marketable debt and equity securities. The Company's pension plan currently has assets with a fair value that is less than the present value of the accumulated benefit obligation under the plan. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $33.4 million and an intangible asset of $6.4 million (representing the amount of unrecognized prior service cost) related to the pension plan. This resulted in a charge to other comprehensive income of $17.6 million, net of taxes.

The Company's pension costs (including the Supplemental Executive Retirement Plan (SERP)) were $10.3 million, $4.8 million and $2.1 million for 2002, 2001 and 2000, respectively. Of these pension costs, approximately 70 percent are expensed and approximately 30 percent are capitalized. The Company's costs for the pension plan are determined in part by actuarial formulas and are dependent upon numerous factors resulting from actual plan experience and assumptions of future experience. Pension costs are affected by actual employee demographics (including age, compensation and the length of service by employees), the amount of cash contributions the Company makes to the pension plan and the return on pension plan assets. Changes made to the provisions of the pension plan may also impact current and future pension costs. Pension plan costs may also be significantly affected by changes in key actuarial assumptions, including the expected return on pension plan assets, the discount rate used in determining the projected benefit obligation and pension costs as well as the assumed rate of increase in employee compensation. The change in pension plan obligations associated with these factors may not be immediately recognized as pension costs in the Consolidated Statement of Income and Comprehensive Income, but generally are recognized in future years over the remaining average service period of pension plan participants. As such, significant portions of pension costs recorded in any period may not reflect the actual level of cash benefits provided to pension plan participants.

The Company has not made any changes to pension plan provisions in 2002, 2001 and 2000 that have had any significant effect on recorded pension plan amounts. The Company has revised the key assumptions of expected return on pension plan assets and the discount rate in 2002 as compared to 2001 and 2000. Such changes had an effect on reported pension costs in 2002 and will have an impact on future years given the cost recognition approach described above. However, in determining pension obligation and costs amounts, these assumptions can change from period to period, and such changes could result in material changes to future pension costs and funding requirements.

The following chart reflects the sensitivities associated with a change in certain actuarial assumptions by the indicated percentage (dollars in thousands):

Actuarial Assumption	Change in Assumption	Impact on Projected Benefit Obligation	Impact on Pension Liability	Impact on Pension Cost
Expected long-term return on plan assets	-0.5%	$ -	$ -*	$769
Expected long-term return on plan assets	+0.5%	-	-*	(770)
Discount rate	-0.5%	17,184	11,450	1,598
Discount rate	+0.5%	(15,396)	(15,396)	(1,411)

* As the Company has already recorded an additional minimum liability for the unfunded accumulated benefit obligation during 2002, changes in the expected return on plan assets would not have an impact on the total pension liability.

In selecting a discount rate, the Company considers yield rates for highly rated corporate bond portfolios with maturities similar to that of the expected term of pension benefits. The Company reduced the discount rate in 2002 from 7.25 percent to 6.75 percent.

In selecting an assumed long-term rate of return on plan assets, the Company considered past performance and economic forecasts for the types of investments held by the plan. The market value of the Company's plan assets has been affected by a decline in equity markets beginning in 2000. For the past three years the fair value of plan assets has decreased \$16.7 million, \$9.3 million and \$1.0 million in 2002, 2001 and 2000, respectively. In its 2002 actuarial valuation, the Company decreased the expected long-term rate of return on plan assets from 9 percent to 8 percent as a result of continued declines in general equity and bond market returns. Reported pension costs are expected to increase in 2003 and future years as the result of this changed assumption. The projected increased pension costs and contributions have been incorporated in the earnings outlook for 2003.

The Company also has a SERP that provides additional pension benefits to executive officers of the Company. The SERP is intended to provide benefits to executive officers whose benefits under the pension plan are reduced due to the application of Section 415 of the Internal Revenue Code of 1986 and the deferral of salary under deferred compensation plans. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of \$0.7 million related to the SERP. In 2001, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of \$1.1 million related to the SERP. This resulted in a charge to other comprehensive income of \$0.5 million and \$0.7 million, net of taxes, for 2002 and 2001, respectively.

The Company provides certain health care and life insurance benefits for substantially all of its retired employees. The Company accrues the estimated cost of postretirement benefit obligations during the years that employees provide services. The Company elected to amortize the transition obligation of \$34.5 million over a period of twenty years, beginning in 1993.

Assumed health care cost trend rates have a significant effect on the amounts reported for the postretirement plans. A one-percentage-point increase in the assumed health care cost trend rate for each year would increase the accumulated postretirement benefit obligation as of December 31, 2002 by \$2.0 million and the service and interest cost by \$0.2 million. A one-percentage-point decrease in the assumed health care cost trend rate for each year would decrease the accumulated postretirement benefit obligation as of December 31, 2002 by \$1.7 million and the service and interest cost by \$0.2 million.

Liquidity and Capital Resources

Review of Cash Flow Statement

Continuing Operating Activities Net cash provided by continuing operating activities was $331.3 million for 2002 compared to net cash used in continuing operating activities of $76.1 million for 2001. The primary reason for the increase in net cash provided by continuing operating activities was power and natural gas cost amortization, net of deferrals and interest, of $68.5 million for 2002 compared to net deferrals of $210.5 million for 2001. This was primarily due to increased retail rates approved by the respective utility commissions to recover increased deferred power and natural gas costs incurred during 2000 and 2001. Net power and natural gas cost amortizations and deferrals are non-cash items that are added back or deducted from net income to determine net cash flows from operating activities using the indirect method. Net cash provided by working capital components was $110.0 million for 2002, compared to $108.3 million of net cash used for 2001. The increase in other current liabilities is primarily due to an increase in deposits held from other parties from $15.7 million as of December 31, 2001 to $92.7 million as of December 31, 2002. Significant changes in non-cash items also included a $57.2 million change in energy commodity assets and liabilities, representing the increase in the unrealized loss on energy trading activities for Energy Trading and Marketing from $30.2 million in 2001 to $87.4 million in 2002. The $119.4 million change in the provision for deferred income taxes was primarily due to changes in deferred power and natural gas cost amortizations and deferrals described above.

Continuing Investing Activities Net cash used in continuing investing activities was $48.3 million for 2002, a decrease compared to $218.4 million for 2001. This was due to a decrease in other capital expenditures and utility property construction expenditures, partially offset by a decrease in the proceeds from property sales and sales of subsidiary investments. Other capital expenditures during 2001 were primarily for the construction of Coyote Springs 2 and the purchase of four turbines by Avista Power that were planned to be used in a non-regulated generation project. In 2001, proceeds from property sales and sale of subsidiary investments were $76.0 million, primarily related to the sale of the 50 percent interest in Coyote Springs 2 and three of Avista Power's turbines. Utility property construction expenditures decreased to $64.2 million for 2002 compared to $119.9 million for 2001.

Continuing Financing Activities Net cash used in continuing financing activities was $284.7 million for 2002 compared to net cash provided of $285.7 million for 2001. During 2002, short-term borrowings decreased $45.1 million and the Company repurchased $203.6 million of long-term debt scheduled to mature in future years. The Company paid net premiums of $9.5 million to repurchase long-term debt in 2002. The decrease in short-term borrowings reflects a decrease in the amount outstanding under Avista Corp.'s line of credit as well as the repayment of a short-term note at Avista Capital. The overall decrease in borrowings during 2002 reflects increased cash flows from operations primarily related to the recovery of deferred power and natural gas costs as well as a general rate increase for Washington electric customers that was partially used to repurchase long-term debt. Cash dividends from Avista Energy were also a significant source of funds used by Avista Corp. to repurchase long-term debt during 2002.

In 2001, the Company issued $550.0 million of long-term debt. During 2001, short-term borrowings decreased $88.1 million, $89.0 million of Medium-Term Notes matured and the Company also legally defeased $50.0 million of Medium-Term Notes scheduled to mature in 2002. The overall increase in borrowings during 2001 was due to increased cash needs to fund capital expenditures and increased power and natural gas costs.

Discontinued Operations Net cash provided by discontinued operations was $16.8 million for 2002 compared to $17.2 million of net cash used in discontinued operations for 2001. The change was primarily due to a decrease in operating costs and capital expenditures by Avista Communications as the Company decided to dispose of the operations. Net cash provided by discontinued operations in 2002 primarily represented the disposal of assets and the settlement of deferred tax assets.

Overall Liquidity

During 2002, the Company's overall liquidity improved compared to 2001. The general electric rate case order issued by the WUTC in June 2002 should allow the Company to continue to improve its liquidity. The general electric rate case order provided for the restructuring and continuation of previously approved rate increases totaling 31.2 percent (a 25 percent temporary surcharge approved in September 2001 and a 6.2 percent increase approved in March 2002). The general increase to base retail rates is 19.3 percent (or $45.7 million in annual revenues) and the remaining 11.9 percent represents the continued recovery of deferred power costs over a period currently projected to extend into 2009. Additionally, the Company has a PCA surcharge of 19.4 percent in place in Idaho. See further details in the section "Avista Utilities - Regulatory Matters."

In addition to rate surcharges and increases, the Company has taken other steps to improve its liquidity. The Company completed the sale of 50 percent of its interest in the Coyote Springs 2 project to Mirant during the fourth quarter of 2001. The Company received $53.6 million in proceeds from Mirant. In addition, Mirant provided the majority of the remaining funds to complete the project. The Company also sold three turbines owned by Avista Power with $22.7 million of proceeds received during the fourth quarter of 2001 and $22.7 million of proceeds received during 2002. Additionally, 2002 operating budgets were designed to control costs and the Company significantly reduced capital expenditures from the amount originally budgeted. The Company's disposal of Avista Communications reduces future cash investments in the Information and Technology line of business. The Company continues discussions with selected companies in its search for a financial partner for Avista Labs with the goal of reducing its ownership interest to less than 20 percent.

Covenants in Avista Energy's credit agreement restrict the amount of cash dividends that can be distributed to Avista Capital and ultimately to Avista Corp. During 2002, in accordance with the modified covenants of its credit agreement, Avista Energy paid $116.4 million in dividends to Avista Capital.

These measures are largely related to the Company's efforts to improve its liquidity and cash flows and should provide the Company the ability to maintain access to adequate levels of credit with its banks.

During the second half of 2000 and the year 2001, the Company's cash outlays for purchased power exceeded the related amounts paid to the Company by its retail customers. This condition was primarily due to the reduced availability of hydroelectric resources compared to historical periods, increased prices in the wholesale market and increased volumes purchased to meet retail customer demand. In addition to operating expenses, the Company has continuing commitments for capital expenditures for construction, improvement and maintenance of facilities. In 2001, the Company incurred substantial levels of indebtedness, both short and long-term, to finance these requirements and to otherwise maintain adequate levels of working capital. Debt service is another significant cash requirement.

If Avista Utilities' power and natural gas costs were to significantly exceed the levels currently recovered from retail customers, its cash flows would be negatively affected. Factors that could cause purchased power costs to exceed the levels currently recovered from customers include, but are not limited to, a return to high prices in wholesale markets combined with an increased need to purchase power in the wholesale markets. Current FERC imposed price caps limit wholesale market prices to $250 per MWh. Factors beyond the Company's control that could result in an increased need to purchase power in the wholesale markets include, but are not limited to, increases in demand (either due to weather or customer growth), low availability of hydroelectric resources, outages at generating facilities and failure of third parties to deliver on energy or capacity contracts.

Capital Resources

The Company incurred significant indebtedness to support capital expenditures, to fund power and natural gas costs that were in excess of the amount recovered currently through rates and to maintain working capital through the end of 2001. However, as of December 31, 2002, the Company's total debt outstanding was $1,004.5 million, a decrease of $248.1 million from $1,252.6 million as of December 31, 2001. The decrease was primarily due to the repurchase of long-term debt and partially due to a decrease in short-term borrowings. This was made possible by improved operating cash flows from both Avista Utilities and Avista Energy. The Company needs to finance capital expenditures and obtain additional working capital from time to time. The cash requirements to service the indebtedness, both short-term and long-term, reduces the amount of cash flow available to fund working capital, purchased power and natural gas costs, capital expenditures, dividends and other corporate requirements.

The Company generally funds capital expenditures with a combination of internally generated cash and external financing. The level of cash generated internally and the amount that is available for capital expenditures fluctuates depending on a variety of factors. Cash provided by utility operating activities and cash generated by Avista Energy are expected to be the Company's primary source of funds for operating needs, dividends and capital expenditures for 2003. Cash flows from operations have improved primarily from the recovery of deferred power and natural gas costs and from the electric rate increase in Washington and the continuation of the PCA surcharge in Idaho. This should allow the Company to continue to reduce total debt outstanding. Capital expenditures are expected to be funded either with cash flows from operations or on an interim basis with short-term borrowings.

On May 21, 2002, the Company entered into a committed line of credit with various banks in the total amount of $225.0 million. The committed line of credit, which expires on May 20, 2003, replaced the $220.0 million committed line of credit that expired on May 29, 2002. As of December 31, 2002, the Company had borrowed $30.0 million under this committed line of credit. Under this committed line of credit, the Company may have up to $50.0 million in letters of credit outstanding. As of December 31, 2002, there was $14.3 million of letters of credit outstanding. The Company's obligation under the committed line of credit is secured with First Mortgage Bonds in the amount of the commitment. The Company is currently in discussions with its banks and believes that the committed line of credit will be renewed for an additional year by the May 20, 2003 expiration date.

The committed line of credit agreement contains customary covenants and default provisions, including covenants not to permit the ratio of "consolidated total debt" to "consolidated total capitalization" of Avista Corp. to be, at the end of any fiscal quarter, greater than 65 percent. As of December 31, 2002, the Company was in compliance with this covenant with a ratio of 54.3 percent. The committed line of credit also has a covenant requiring the ratio of "earnings before interest, taxes, depreciation and amortization" to "interest expense" of Avista Utilities for the year ending December 31, 2002 to be greater than 1.6 to 1. As of December 31, 2002, the Company was in compliance with this covenant with a ratio of 2.04 to 1.

Any default on its committed line of credit or other financing arrangements could result in cross-defaults to other agreements and could induce vendors and other counterparties to demand collateral. In the event of default, it would be difficult for the Company to obtain financing on any reasonable terms to pay creditors or fund operations, and the Company would likely be prohibited from paying dividends on its common stock. As of December 31, 2002, Avista Corp. was in compliance with the covenants of all of its financing agreements.

During 2002, the Company repurchased $133.8 million of Medium-Term Notes scheduled to mature in 2003, $59.8 million of Unsecured Senior Notes scheduled to mature in 2008 and $10.0 million of Medium-Term Notes scheduled to mature in 2028. In accordance with regulatory accounting practices under SFAS No. 71, total net premiums paid to repurchase debt were $9.5 million and are being amortized over the average remaining maturity of outstanding debt.

The Mortgage and Deed of Trust securing the Company's First Mortgage Bonds contains limitations on the amount of First Mortgage Bonds which may be issued based on, among other things, a 70 percent debt-to-collateral ratio and a 2.00 to 1 net earnings to First Mortgage Bond interest ratio. Under various financing agreements, the Company is also restricted as to the amount of additional First Mortgage Bonds that it can issue. As of December 31, 2002, the Company could issue $109.4 million of additional First Mortgage Bonds under the most restrictive of these financing agreements.

If market conditions warrant during 2003, the Company may issue long-term debt and repurchase outstanding long-term debt to reduce its overall debt service costs.

The Company is restricted under various agreements and its Restated Articles of Incorporation as to the additional preferred stock it can issue. As of December 31, 2002, approximately $267.1 million of additional preferred stock could be issued at an assumed dividend rate of 6.95 percent with a maturity date later than June 1, 2008.

In July 2001, the Company filed a registration statement on Form S-3 with the Securities and Exchange Commission for the purpose of issuing up to 3.7 million shares of common stock. No common stock has been issued and the Company currently does not have any plans to issue common stock under this registration statement.

Inter-Company Debt; Subordination

As part of its on-going cash management practices and operations, Avista Corp. from time to time makes unsecured short-term loans to, and borrowings from, Avista Capital. In turn, Avista Capital from time to time makes unsecured short-term loans to, and borrowings from, its subsidiaries. As of December 31, 2002, Avista Corp. held short-term notes of Avista Capital in the principal amount of $137.3 million; and Avista Capital held, among other notes, $109.0 million in principal amount of short-term notes of Avista Power, issued primarily for the construction of Coyote Springs 2. The inter-company borrowings associated with Coyote Springs 2 were satisfied with the transfer of the interest in the plant from Avista Power to Avista Corp. in January 2003.

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

The credit arrangements of Avista Capital's subsidiaries generally provide that any indebtedness owed by such entity to its corporate parent will be subordinated to the indebtedness outstanding under such credit arrangements.

The right of Avista Corp., as a shareholder, to receive assets of any of its direct or indirect subsidiaries upon the subsidiary's liquidation or reorganization (and the consequent right of the holders of debt securities and other creditors of Avista Corp. to participate in those assets) is junior to the claims against such assets of that subsidiary's creditors. As a result, the obligations of Avista Corp. to its debt securityholders and other unrelated creditors are effectively subordinated in right of payment to all indebtedness and other liabilities and commitments (including trade payables and lease obligations) of Avista Corp.'s direct and indirect subsidiaries. Similarly, the obligations of Avista Capital to its creditors are effectively subordinated in right of payment to all indebtedness and other liabilities and commitments of its direct and indirect subsidiaries.

Pension Plan

As of December 31, 2002, the Company's pension plan had assets with a fair value that was less than the present value of the accumulated benefit obligation under the plan. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $33.4 million and an intangible asset of $6.4 million (representing the amount of unrecognized prior service cost) related to the pension plan. This resulted in a charge to other comprehensive income of $17.6 million, net of taxes. The Company does not expect the current pension plan funding deficit to have a material adverse impact on its financial condition, results of operations or cash flows. The Company's funding policy is to contribute amounts that are not less than the minimum amounts required to be funded under the Employee Retirement Income Security Act. The Company made $12 million in cash contributions to the pension plan in 2002 and did not make any cash contributions to the pension plan in 2001. The Company expects to contribute approximately $12 million to the pension plan in 2003. The Company is funding the pension plan at what it believes to be an adequate level. The increased funding and pension costs have been factored into the Company's earnings outlook for 2003.

Off-Balance Sheet Arrangements

Avista Receivables Corp. (ARC), formerly known as WWP Receivables Corp., is a wholly owned, bankruptcy-remote subsidiary of the Company formed in 1997 for the purpose of acquiring or purchasing interests in certain accounts receivable, both billed and unbilled, of the Company. On May 29, 2002, ARC, the Company and a third-party financial institution entered into a three-year agreement whereby ARC can sell without recourse, on a revolving basis, up to $100.0 million of those receivables. ARC is obligated to pay fees that approximate the purchaser's cost of issuing commercial paper equal in value to the interests in receivables sold. As of December 31, 2002, $65.0 million in receivables were sold pursuant to the agreement. ARC will not be consolidated in accordance with a recently issued FASB interpretation related to special-purpose entities.

WP Funding LP is an entity that was formed for the purpose of acquiring the natural gas-fired combustion turbine generating facility in Rathdrum, Idaho (Rathdrum CT). WP Funding LP purchased the Rathdrum CT from the Company with funds provided by unrelated investors of which 97 percent represented debt and 3 percent represented equity. The Company operates the Rathdrum CT and leases it from WP Funding LP and currently makes lease payments of $4.5 million per year. The total amount of WP Funding LP debt outstanding that is not included on the Company's balance sheet was $54.5 million as of December 31, 2002. The lease term expires in February 2020; however, the current debt matures in October 2005 and will need to be refinanced at that time. The FASB has issued an interpretation relating to the identification of, and accounting for, special-purpose entities such as WP Funding LP. See "Note 2 of the Notes to Consolidated Financial Statements" for further information. This interpretation will require the Company to begin consolidating WP Funding LP into its financial statements effective July 1, 2003, whereby the $54.5 million of debt will be included in the Company's capitalization and the book value of the Rathdrum CT will be included in utility plant. The equity investment of the unrelated investors will be reported as a minority interest. Based on current information, the difference between the book value of the debt and equity of WP Funding LP and the book value of the Rathdrum CT is approximately $15.5 million ($10.1 million, net of taxes). The Company intends to request regulatory accounting orders to record this amount as a regulatory asset upon the consolidation of WP Funding LP.

Total Company Capitalization

The Company's consolidated capital structure, including the current portion of long-term debt and short-term borrowings was 54.3 percent debt, 5.4 percent preferred trust securities, 1.8 percent preferred stock and 38.5 percent common equity as of December 31, 2002, compared to 59.4 percent debt, 4.7 percent preferred trust securities, 1.7 percent preferred stock and 34.2 percent common equity as of December 31, 2001. The Company's consolidated debt decreased by $248 million due to both the repurchase of long-term debt and a decrease in short-term borrowings. The Company's consolidated common equity decreased $7.3 million during 2002 to $712.8 million as of December 31,

2002. This decrease is primarily due to dividends and other comprehensive loss, partially offset by net income and the issuance of common stock through the Dividend Reinvestment Plan and employee benefit plans. The significant other comprehensive loss of $20.3 million for 2002 was primarily related to the recording of an unfunded accumulated benefit obligation for the pension plan. The Company has a target capital structure of 50 percent total debt and 50 percent preferred trust securities, preferred stock and common equity. The Company plans to achieve this capital structure primarily with the reduction of total debt and the retention of net earnings.

Credit Ratings

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

	Standard & Poor's	Moody's	Fitch, Inc.
Avista Corporation			
Corporate/Issuer rating	BB+	Ba1	BB+
Senior secured debt	BBB-	Baa3	BBB-
Senior unsecured debt	BB+	Ba1	BB+
Preferred stock	BB-	Ba3	BB
Avista Capital I*			
Preferred Trust Securities	BB-	Ba2	BB+
Avista Capital II*			
Preferred Trust Securities	BB-	Ba2	BB
Rating outlook	Stable**	Negative	Stable

* Only assets are subordinated debentures of Avista Corporation

** Changed to stable from negative on December 18, 2002

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

Avista Utilities Operations

Capital expenditures for Avista Utilities were $282.8 million for the 2000-2002 period. This excludes Coyote Springs 2, which was included in Energy Trading and Marketing. During the 2003-2005 period, utility capital expenditures are expected to be in the range of $90 to $110 million per year and long-term debt maturities and preferred stock sinking fund requirements total $137 million. During this period, internally generated funds and short-term borrowing arrangements are expected to be sufficient to fund the Company's capital expenditures, maturing long-term debt and preferred stock sinking fund requirements. These estimates of capital expenditures are subject to continuing review and adjustment. Actual capital expenditures may vary from these estimates due to factors such as changes in business conditions, construction schedules and environmental requirements.

Avista Utilities' planned capital expenditures include an expansion and enhancement of its 230 kV transmission system at an estimated total cost of $85 to $100 million that is expected to be completed by the end of 2006. To the extent that Avista Utilities chooses to or is required to divest of its transmission assets, it would expect to recover these costs.

Avista Utilities held cash deposits from other parties in the amount of $17.5 million as of December 31, 2002, which is included in cash and cash equivalents with a corresponding amount in other current liabilities in the Consolidated Balance Sheet. These amounts are subject to return if conditions warrant because of continuing portfolio value fluctuations with those parties or substitution of collateral.

As of December 31, 2002, Avista Utilities had $37.0 million in cash and temporary investments, including the $17.5 million of cash deposits from other parties.

See "Notes 6, 15, 16, 17, 20, 21, 22, 23 and 24 of Notes to Consolidated Financial Statements" for additional details related to financing activities.

Energy Trading and Marketing Operations

Avista Energy funds its ongoing operations with a combination of internally generated cash and a bank line of credit. On June 28, 2002 Avista Energy and its subsidiary, Avista Energy Canada, Ltd., as co-borrowers, renewed their credit agreement with a group of banks in the aggregate amount of $110.0 million expiring June 30, 2003. This credit agreement may be terminated by the banks at any time and all extensions of credit under the agreement are payable upon demand, in either case at the lenders' sole discretion. This agreement also provides, on an uncommitted basis, for the issuance of letters of credit to secure contractual obligations to counterparties. This facility is guaranteed by Avista Capital and secured by Avista Energy's assets. The maximum amount of credit extended by the banks for the issuance of letters of credit is the subscribed amount of the facility less the amount of outstanding cash advances, if any. The maximum amount of credit extended by the banks for cash advances is $30.0 million. As of December 31, 2002, there were no cash advances (demand notes payable) outstanding and letters of credit outstanding under the facility totaled $17.4 million.

The Avista Energy credit agreement contains customary covenants and default provisions, including covenants to maintain "minimum net working capital" and "minimum net worth" as well as a covenant limiting the amount of indebtedness which the co-borrowers may incur. Avista Energy was in compliance with the covenants of its credit agreement as of December 31, 2002.

Avista Energy believes that it will have access to credit facilities beyond the June 30, 2003 expiration date of its current uncommitted credit agreement.

Avista Capital provides guarantees for Avista Energy's credit agreement and, in the course of business, may provide guarantees to other parties with whom Avista Energy may be doing business. Avista Capital had $64.6 million of performance guarantees related to energy trading contracts outstanding as of December 31, 2002.

Periodically, Avista Capital may lend funds to Avista Energy to support its short-term cash and collateral needs. Avista Energy's obligations to repay loans to Avista Capital are subordinate to any obligations of Avista Energy to the banks under the credit agreements. As of December 31, 2002, there were no loans between Avista Capital and Avista Energy outstanding.

Avista Energy manages collateral requirements with counterparties by providing letters of credit, providing guarantees from Avista Capital, cash deposited with counterparties and offsetting transactions with counterparties. Cash deposited with counterparties totaled $35.7 million as of December 31, 2002, and is included in prepayments and other current assets in the Consolidated Balance Sheet. Avista Energy held cash deposits from other parties in the amount of $75.2 million as of December 31, 2002, which is included in cash and cash equivalents with a corresponding amount in other current liabilities in the Consolidated Balance Sheet. These amounts are subject to return if conditions warrant because of continuing portfolio value fluctuations with those parties or substitution of collateral.

As of December 31, 2002, Avista Energy had $148.9 million in cash, including the $75.2 million of cash deposits from other parties. Covenants in Avista Energy's credit agreement restrict the amount of cash dividends that can be distributed to Avista Capital and ultimately to Avista Corp. During 2002, in accordance with the modified covenants of its credit agreement, Avista Energy paid $116.4 million in dividends to Avista Capital. In January 2003, Avista Energy paid $2.1 million in dividends to Avista Capital.

Capital expenditures for the Energy Trading and Marketing companies were $239.6 million for the 2000-2002 period, primarily due to Avista Power's investment in Coyote Springs 2 as well as the purchase of turbines during 2001. Capital expenditures are expected to be less than $1.0 million per year in this line of business during the 2003-2005 period.

Information and Technology Operations

Capital expenditures for the Information and Technology line of business were $14.7 million for the 2000-2002 period. The 2003-2005 capital expenditures are expected to be between $3.0 and $4.0 million per year. Avista Advantage and Avista Labs expect to support these capital requirements through a combination of funding from Avista Corp. and third party equity investment. Two venture capital firms made minority interest investments totaling $3.4 million in Avista Advantage during the fourth quarter of 2000. As of December 31, 2002, the Information and Technology companies had $0.1 million in cash and cash equivalents and $0.6 million in debt outstanding. The Company continues discussions with selected companies in its search for a financial partner for Avista Labs with the goal of reducing its ownership interest in Avista Labs to less than 20 percent.

Other Operations

Capital expenditures for these companies were $1.8 million for the 2000-2002 period. The 2003-2005 capital expenditures are not expected to be material. As of December 31, 2002, this line of business had $0.4 million in cash and cash equivalents and temporary investments, with $0.2 million in debt outstanding. In October 2001, Avista Capital entered into a one-year $20 million promissory note collateralized by certain receivables. The note was extended in October 2002 and paid off in December 2002.

Contractual Obligations

The following table provides a summary of the Company's future contractual obligations as of December 31, 2002 (dollars in millions):

	2003	2004	2005	2006	2007	Thereafter
Avista Utilities:						
Long-term debt maturities	$ 71	$ 30	$ 30	$ 38	$ 26	$ 780
Short-term debt (1)	95	-	-	-	-	-
Preferred stock redemptions	2	2	2	2	25	-
Preferred trust securities	-	-	-	-	-	100
Energy purchase contracts (2)	390	290	148	113	115	892
Public Utility District contracts (2)	4	3	3	3	3	22
Operating lease obligations (3)	12	10	7	7	7	65
Capital lease obligations (3)	-	-	-	-	-	-
Other obligations (4)	10	12	12	12	12	185
Avista Capital (consolidated):						
Long-term debt maturities	1	-	-	-	-	-
Physical energy contracts (5)	936	324	206	188	126	393
Financial energy contracts (5)	961	89	3	12	-	-
Operating lease obligations (3)	3	3	2	1	-	1
Capital lease obligations (3)	1	-	-	-	-	-
Total cash requirements	$2,486	$763	$413	$376	$314	$2,438

(1) Represents $30 million outstanding under a $225 million line of credit and $65 million outstanding under a $100 million accounts receivable financing facility.
(2) All of the energy purchase contracts were entered into as part of Avista Utilities' obligation to serve its retail natural gas and electric customers' energy requirements. As a result, these costs are generally recovered either through base retail rates or adjustments to retail rates as part of the power and natural gas cost adjustment mechanisms.
(3) Includes the interest component of the lease obligation.
(4) Represents operational agreements, settlements and other contractual obligations with respect to generation, transmission and distribution facilities.
(5) Represents Avista Energy's contractual commitments under energy contracts in future periods. Avista Energy also has sales commitments related to energy commodities in future periods.

As of December 31, 2002, Avista Corp. did not have any commitments outstanding with equity triggers. When the Company's corporate credit rating was reduced to below investment grade in October 2001, additional collateral requirements due to rating triggers were met and further requirements are not currently anticipated. The Company does not expect any material impact from rating triggers; remaining triggers primarily relate to changes in pricing under certain financing agreements.

Additional Financial Data

As of December 31, 2002, the total long-term debt of the Company and its consolidated subsidiaries, as shown in the Company's consolidated financial statements, was $902.6 million. Of such amount, $605.3 million represents long-term unsecured and unsubordinated indebtedness of the Company, and $298.5 million represents secured indebtedness of the Company. The unamortized debt discount was $2.2 million. Other long-term debt was $1.0 million. Consolidated long-term debt does not include the Company's subordinated indebtedness held by the issuers of Company-obligated preferred trust securities. In addition to long-term secured indebtedness, $30.0 million of the

Company's short-term debt outstanding under or backed by its $225.0 million committed line of credit is secured indebtedness. The current portion of long-term debt was $71.9 million as of December 31, 2002, of which $15.0 million was secured indebtedness.

Future Outlook

Business Strategy

Avista Corp. intends to continue to focus on its core energy-related businesses. Avista Corp. intends to focus on improving cash flows and earnings, controlling costs and reducing debt while working to restore an investment grade credit rating. Avista Utilities seeks to maintain a strong, low-cost and efficient electric and natural gas utility business focused on providing reliable, high quality service to its customers. The utility business is expected to grow modestly, consistent with historical trends. Expansion is expected to result primarily from economic growth in its service territory. It is Avista Utilities' strategy to own or control a sufficient amount of resources to meet its retail and wholesale energy requirements on an average annual basis. Avista Energy works primarily within the WECC and focuses on asset-backed optimization of combustion turbines and hydroelectric assets owned by other entities, long-term electric supply contracts, natural gas storage, and electric and natural gas transmission and transportation arrangements. Avista Energy's marketing efforts are driven by its base of knowledge and experience in the operation of both electric energy and natural gas physical systems in the WECC, as well as its relationship-focused approach with its customers. Avista Advantage remains focused on growing revenue, improving margins, reducing fixed and variable costs and improving client satisfaction. Avista Corp. continues discussions with selected companies in its search for a financial partner for Avista Labs with the goal of owning less than 20 percent of this company. Avista Labs continues to move forward with developing and selling its commercial fuel cell products. The Company plans to dispose of assets and phase out of operations in the Other business segment that are not related to its energy operations.

Competition

Avista Utilities competes to provide service to new retail electric customers with various rural electric cooperatives and public utility districts in and adjacent to its service territories. Alternate providers of power may also compete for sales to existing customers, including new market entrants as a result of deregulation. Competition for available electric resources can be critical to utilities as surplus power resources are absorbed by load growth. Avista Utilities' natural gas distribution operations compete with other energy sources; however, natural gas continues to maintain a price advantage compared to heating oil, propane and other fuels, provided that the natural gas distribution system is proximate to prospective customers.

The Energy Policy Act of 1992 (Energy Act) amended provisions of the Public Utility Holding Company Act of 1935 (PUHCA) and the Federal Power Act to remove certain barriers to a competitive wholesale market. The Energy Act expanded the authority of the FERC to issue orders requiring electric utilities to transmit power and energy to or for wholesale purchasers and sellers, and to require electric utilities to enlarge or construct additional transmission capacity for the purpose of providing these services. It also created "exempt wholesale generators," a new class of independent power plant owners that are able to sell generation only at the wholesale level. This permits public utilities and other entities to participate through subsidiaries in the development of independent electric generating plants for sales to wholesale customers without being required to register under the PUHCA.

Participants in the wholesale market include other utilities, federal marketing agencies and energy trading and marketing companies. The wholesale market has changed significantly over the last few years with respect to market participants involved, level of activity, variability in market prices, liquidity, FERC imposed price caps and counterparty credit issues. During 2000 and the first half of 2001, the electric wholesale market in the WECC region was more turbulent than previously experienced and marked by significant volatility, service disruptions and defaults by certain participants. During the second half of 2001 and 2002 wholesale market prices decreased to levels similar to those experienced before 2000. Many energy companies are facing liquidity issues, and counterparty credit exposure is of concern to all market participants. During 2002, electric and natural gas trading volumes have decreased, the energy markets are less volatile and fewer creditworthy counterparties are currently participating in the energy markets. Avista Corp. is actively monitoring energy industry developments with a focus on liquidity, volatility of energy trading markets and counterparty credit exposure.

The Avista Capital subsidiaries, particularly the Information and Technology companies, are subject to competition as they develop products and services and enter new markets. Competition from other companies in these emerging industries may mean challenges for a company to be the first to market a new product or service to gain the advantage in market share. In order for these new businesses to grow as planned, one significant challenge will be the availability of funding and resources to meet the capital needs. Other challenges will be rapidly advancing technologies, possibly making some of the current technology quickly obsolete, and requiring continual research and development for product advancement. In order for some of these subsidiaries to succeed, they will need to reduce costs of these emerging technologies to make them affordable to future customers.

Business Risk

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

As described under "Avista Corp. Lines of Business," hydroelectric conditions in 2001 were significantly below normal, leading to greater than normal reliance on purchased power. Hydroelectric generation was slightly above normal in 2002 and current forecasts indicate that hydroelectric generation will be approximately 83 percent of normal in 2003. The earnings impact of these factors is mitigated by regulatory mechanisms that are intended to defer increased power supply costs for recovery in future periods. Avista Utilities is not able to fully predict how the combination of energy resources, energy loads, prices, rate recovery and other factors will ultimately drive deferred power costs and the timing of recovery of these costs in future periods. Current estimates and projections by the Company indicate that deferred power costs will be recovered by 2009. See further information at "Avista Utilities - Regulatory Matters."

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

Natural gas commodity prices increased dramatically during 2000 and remained at relatively high levels during the first half of 2001 before declining in the second half of the year. Natural gas commodity prices during 2002 were generally lower than during 2000 and the first half of 2001. Natural gas commodity prices have increased towards the end of 2002 and into 2003. Market prices for natural gas continue to be competitive compared to alternative fuel sources for residential, commercial and industrial customers. Avista Utilities believes that natural gas should sustain its market advantage based on the levels of existing reserves and the potential for natural gas development in the future. Growth has occurred in the natural gas business in recent years due to increased demand for natural gas in new construction, as well as conversions from electric space, oil space and electric water heating to natural gas. Challenges facing Avista Utilities' natural gas operations include, among other things, volatility in the price of natural gas, changes in the availability of natural gas, legislative and governmental regulations, weather conditions and the timing of recovery for increased commodity costs. Avista Utilities' natural gas business also faces the potential for large natural gas customers to by-pass its natural gas system. To reduce the potential for such by-pass, Avista Utilities prices its natural gas services, including transportation contracts, competitively and has varying degrees of flexibility to price its transportation and delivery rates by means of individual contracts, subject to state regulatory review and approval. Avista Utilities has long-term transportation contracts with seven of its largest industrial customers, which reduces the risk of these customers by-passing the system in the foreseeable future.

Avista Energy trades electricity and natural gas, along with derivative commodity instruments, including futures, options, swaps and other contractual arrangements. As a result of these trading activities, Avista Energy is subject to various risks, including commodity price risk and credit risk, as well as possible new risks resulting from the recent imposition of market controls by federal and state agencies. The FERC is conducting separate proceedings related to market controls within California and within the Pacific Northwest that include proposals by certain parties to retroactively impose price caps. As a result, certain parties have asserted claims for significant refunds from Avista Energy and lesser refunds from Avista Utilities which could result in liabilities for refunding revenues recognized in prior periods. Avista Energy and Avista Utilities have joined other parties in opposing these proposals. The California proceedings provide that any refunds owed could be offset against unpaid energy debts due to the same party. Avista Energy has fully reserved for all defaulted obligations from California parties and believes that any refunds imposed would not exceed its uncollected receivables. If retroactive price caps or refunds were imposed in the Pacific Northwest, Avista Energy and Avista Utilities could assert offsetting claims for certain transactions. See "Power Market Issues" for further information with respect to the FERC refund proceedings.

In connection with matching loads and resources, Avista Utilities engages in wholesale sales and purchases of electric capacity and energy and, accordingly, is also subject to commodity price risk, credit risk and other risks associated with these activities.

Commodity Price Risk. Both Avista Utilities and Avista Energy are subject to energy commodity price risk. The price of power in wholesale markets is affected primarily by production costs and by other factors including streamflows, the availability of hydroelectric and thermal generation and transmission capacity, weather and the resulting retail loads, and the price of coal, natural gas and oil to operate thermal generating units. Any combination of these factors that results in a shortage of energy generally causes the market price of power to move upward. Additionally, the FERC imposed a price mitigation plan in the western United States in June 2001.

Price risk is, in general, the risk of fluctuation in the market price of the commodity needed, held or traded. In the case of electricity, prices can be affected by the adequacy of generating reserve margins, scheduled and unscheduled outages of generating facilities, availability of streamflows for hydroelectric generation, the price of thermal generating plant fuel, and disruptions or constraints to transmission facilities. Demand changes (caused by variations in the weather and other factors) can also affect market prices. Price risk also includes the risk of fluctuation in the market price of associated derivative commodity instruments (such as options and forward contracts). Price risk may also be influenced to the extent that the performance or non-performance by market participants of their contractual obligations and commitments affect the supply of, or demand for, the commodity. Wholesale market prices for power and natural gas in the western United States and western Canada were significantly higher in 2000 and the first half of 2001 than at any time in history, with unprecedented levels of volatility. Prices and volatility decreased considerably during the second half of 2001 and 2002 relative to 2000 and the first half of 2001.

Credit Risk. Credit risk relates to the risk of loss that Avista Utilities and/or Avista Energy would incur as a result of non-performance by counterparties of their contractual obligations to deliver energy and make financial settlements. Credit risk includes not only the risk that a counterparty may default due to circumstances relating directly to it, but also the risk that a counterparty may default due to circumstances that relate to other market participants that have a direct or indirect relationship with such counterparty. Avista Utilities and Avista Energy seek to mitigate credit risk by applying specific eligibility criteria to existing and prospective counterparties and by actively monitoring current credit exposures. These policies include an evaluation of the financial condition and credit ratings of counterparties, collateral requirements or other credit enhancements, such as letters of credit or parent company guarantees, and the use of standardized agreements that allow for the netting or offsetting of positive and negative exposures associated with a single counterparty. However, despite mitigation efforts, defaults by counterparties periodically occur. Avista Energy experienced payment receipt defaults from certain parties impacted by the California energy crisis. Avista Energy and Avista Corp. (through the Avista Utilities division) have engaged in physical and financial transactions with Enron Corporation (Enron) and certain of its affiliates and experienced disruptions to forward contract commitments as a result of Enron's December 2001 bankruptcy. The Enron bankruptcy and other changes, uncertainties and regulatory proceedings have resulted in reduced liquidity in the energy markets. See "Enron Corporation" in "Note 28 of Notes to Consolidated Financial Statements" for more information.

A trend of declining credit quality was evident during 2002, particularly in the energy industry. Rating agencies have downgraded the credit ratings of several of the counterparties of Avista Energy and Avista Utilities. Avista Energy and Avista Utilities regularly evaluate counterparties' credit exposure for future settlements and delivery obligations. Avista Energy and Avista Utilities have taken a conservative position by reducing or eliminating open (unsecured) credit limits for parties perceived to have increased default risk. Counterparty collateral is used to offset the Company's credit risk where unsettled net positions and future obligations by counterparties to pay Avista Utilities and/or Avista Energy or deliver to Avista Utilities and/or Avista Energy warrant.

Avista Energy has concentrations of suppliers and customers in the electric and natural gas industries including electric utilities, natural gas distribution companies, and other energy marketing and trading companies. In addition, Avista Energy has concentrations of credit risk related to geographic location as Avista Energy operates in the western United States and western Canada. These concentrations of counterparties and concentrations of geographic location may impact Avista Energy's overall exposure to credit risk, either positively or negatively, in that the counterparties may be similarly affected by changes in economic, regulatory or other conditions.

Credit risk also involves the exposure that counterparties perceive related to performance by Avista Utilities and Avista Energy to perform deliveries and settlement of energy transactions. These counterparties may seek assurance of performance in the form of letters of credit, prepayment or cash deposits, and, in the case of Avista Energy, parent company performance guarantees. In periods of price volatility, the level of exposure can change significantly, with the result that sudden and significant demands may be made against the Company's capital resource reserves (credit facilities and cash). Avista Utilities and Avista Energy actively monitor the exposure to possible collateral calls and take steps to minimize capital requirements.

In conjunction with the valuation of their commodity derivative instruments and accounts receivable, Avista Utilities and Avista Energy maintain credit reserves that are based on management's evaluation of the credit risk of the overall portfolio. Based on these policies, exposures and credit reserves, the Company does not anticipate a materially adverse effect on its financial condition or results of operations as a result of counterparty nonperformance.

Other Operating Risks. In addition to commodity price risk, Avista Utilities' commodity positions are subject to operational and event risks including, among others, increases in load demand, transmission or transport disruptions, fuel quality specifications, forced outages at generating plants and disruptions to information systems and other administrative tools required for normal operations. Avista Utilities also has exposure to weather conditions and natural disasters that can cause physical damage to property, requiring immediate repairs to restore utility service.

The emergence of terrorism threats, both domestic and foreign, is a risk to the entire utility industry, including Avista Utilities. Potential disruptions to operations or destruction of facilities from terrorism are not readily determinable. The Company has taken various steps to mitigate terrorism risks and to prepare contingency plans in case its facilities are targeted.

Interest Rate Risk. The Company is subject to the risk of fluctuating interest rates in the normal course of business. The Company manages interest rate risk by taking advantage of market conditions when timing the issuance of long-term financings and optional debt redemptions and through the use of fixed rate long-term debt with varying maturities. The interest rate on $40 million of Company-Obligated Mandatorily Redeemable Preferred Trust Securities - Series B is adjusted quarterly, reflecting current market conditions. In order to lower interest payments during a period of declining interest rates, Avista Corp. entered into an interest rate swap agreement, effective July 17, 2002, that terminates on June 1, 2008. This interest rate swap agreement effectively changes the interest rate on $25 million of Unsecured Senior Notes from a fixed rate of 9.75 percent to a variable rate based on LIBOR. Additionally, amounts borrowed under the Company's $225.0 million line of credit have a variable interest rate.

The Company's credit ratings were downgraded during the fourth quarter of 2001 resulting in an overall corporate credit rating that is below investment grade. These downgrades increased the cost of debt and other securities going forward and may affect the Company's ability to issue debt and equity securities at reasonable interest rates and prices. The downgrades also required the Company to provide letters of credit and/or collateral to certain parties.

Foreign Currency Risk. The Company has investments in Canadian companies through Avista Energy Canada, Ltd. and its subsidiary, Copac Management, Inc. The Company's exposure to foreign currency risk and other foreign operations risk was immaterial to the Company's consolidated results of operations and financial position during 2002 and is not expected to change materially in the near future.

Risk Management

Risk Policies and Oversight. Avista Utilities and Avista Energy use a variety of techniques to manage risks. The Company has risk management oversight for these risks for each area of the Company's energy-related businesses. The Company has a Risk Management Committee, separate from the units that create such risk exposure and that is overseen by the Audit Committee of the Company's Board of Directors, to monitor compliance with the Company's risk management policies and procedures. Avista Utilities and Avista Energy have policies and procedures in place to manage the risks, both quantitative and qualitative, inherent in their businesses. The Company's Risk Management Committee reviews the status of risk exposures through regular reports and meetings and it monitors compliance with the Company's risk management policies and procedures on a regular basis. Nonetheless, adverse changes in commodity prices, generating capacity, customer loads, regulation and other factors may result in losses in earnings, cash flows and/or fair values.

Quantitative Risk Measurements. Avista Utilities has volume limits for its imbalance between projected loads and resources. Normal operations result in seasonal mismatches between power loads and available resources. Avista Utilities is able to vary the operation of its generating resources to help match hourly, daily and weekly load fluctuations. Avista Utilities uses the wholesale power markets to sell projected resource surpluses and obtain resources when deficits are projected in the 18-month forward planning horizon. Any imbalance is required to remain within limits, or management action or decisions are triggered to address larger imbalance situations. Volume limits for forward periods are based on monthly and quarterly averages that may vary materially from the actual load and resource variations within any given month or operating day. Future projections of resources are updated as forecasted streamflows and other factors differ from prior estimates. Forward power markets may be illiquid, and market products available may not match Avista Utilities' desired transaction size and shape. Therefore, open imbalance positions exist at any given time.

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

The VAR computations are based on a historical simulation, utilizing price movements over a specified period to simulate forward price curves in the energy markets to estimate the potential unfavorable impact of price movement in the portfolio of transactions scheduled to settle within the following eight calendar quarters. The quantification of market risk using VAR provides a consistent measure of risk across Avista Energy's continually changing portfolio. VAR represents an estimate of reasonably possible net losses in earnings that would be recognized on its portfolio assuming hypothetical movements in future market rates and is not necessarily indicative of actual results that may occur.

Avista Energy's VAR computations utilize several key assumptions, including a 95 percent confidence level for the resultant price movement and holding periods of one and three days. The calculation includes derivative commodity instruments held for trading purposes and excludes the effects of embedded physical options in the trading portfolio.

As of December 31, 2002, Avista Energy's estimated potential one-day unfavorable impact on net margin was $0.7 million, as measured by VAR, related to its commodity trading and marketing business, compared to $0.4 million as of December 31, 2001. The average daily VAR for 2002 was $0.6 million. Avista Energy was in compliance with its one-day VAR limits during 2002. Changes in markets inconsistent with historical trends or assumptions used could cause actual results to exceed predicted limits. Market risks associated with derivative commodity instruments held for purposes other than trading were not material as of December 31, 2002.

For forward transactions that settle beyond the next eight calendar quarters, Avista Energy applies other risk measurement techniques, including price sensitivity stress tests, to assess the future market risk. Volatility in longer-dated forward markets tends to be significantly less than near-term markets.

Economic and Load Growth

Avista Utilities, along with others in the service area, is continuing its efforts to facilitate expansion of existing businesses and to attract new businesses to the Inland Northwest. Agriculture, mining and lumber were the primary industries for many years; today health care, education, financial, electronic and other manufacturing, tourism and the service sectors have become important industries that operate in Avista Utilities' service area. Avista Utilities also anticipates moderate economic growth to continue in its Oregon service area.

Avista Utilities anticipates residential and commercial electric load growth to average between 2.5 and 3.5 percent annually for the next four years, primarily due to increases in both population and the number of businesses in its service territory. The number of electric customers is expected to increase and the average annual usage by residential customers is expected to remain steady.

Avista Utilities anticipates natural gas load growth to average between 3.0 and 4.0 percent annually for the next four years. The anticipated natural gas load growth is primarily due to expected conversions from electric space, oil space and electric water heating to natural gas, and increases in both population and the number of businesses in its service territory.

During 2001 and 2002, Avista Utilities experienced decreased loads and decreased use per customer with respect to both electric and natural gas retail sales. The decrease in use per customer appears to be primarily due to a response to the increase in rates and the resulting conservation efforts of individual customers. The decrease in use per customer in 2002 and 2001 as compared to 2000 also appears to reflect milder weather in 2002 and 2001 as compared to 2000. The decrease in total kWhs and therms sold primarily relates to industrial customers and appears to reflect a general downturn in the economy of the Company's service territory. However, as described above, based on economic forecasts, publicly available studies and internal analysis of company-specific data, the Company does not expect the trend of declining loads to continue over the next four years.

The forward-looking projections set forth above regarding retail sales growth are based, in part, upon purchased economic forecasts and publicly available population and demographic studies. The expectations regarding retail sales growth are also based upon various assumptions including, without limitation, assumptions relating to weather and economic and competitive conditions, internal analysis of company-specific data, such as energy consumption patterns and internal business plans, and an assumption that Avista Utilities will incur no material loss of retail customers due to self-generation or retail wheeling. Changes in the underlying assumptions can cause actual experience to vary significantly from forward-looking projections.

Information Services Contract

Electronic Data Systems (EDS) has performed certain information services for the Company since 1992. The Company's current contract with EDS expires in August 2005. In order to increase flexibility and increase efficiencies, the Company is currently negotiating to extend and restructure its contract with EDS. The Company believes that any changes to the contract with EDS will not have any material impact on its financial condition or results of operations and will not result in any disruption to its business operations.

Environmental Issues

Since December 1991, a number of species of fish in the Northwest, including the Snake River sockeye salmon and fall chinook salmon, the Kootenai River white sturgeon, the upper Columbia River steelhead, the upper Columbia River spring chinook salmon and the bull trout, have been listed as threatened or endangered under the Federal Endangered Species Act. Thus far, measures that were adopted and implemented to save the Snake River sockeye salmon and fall chinook salmon have not directly impacted generation levels at any of Avista Utilities' hydroelectric dams. Avista Utilities does, however, purchase power from four projects on the Columbia River that are directly impacted by ongoing mitigation measures for salmon and steelhead. The reduction in generation at these projects is relatively minor, resulting in minimal economic impact on Avista Utilities at this time. It is currently not possible to accurately predict the likely economic costs to the Company resulting from all future actions.

The Company received a new FERC operating license for the Cabinet Gorge and Noxon Rapids hydroelectric projects in March 2001 that incorporates a comprehensive settlement agreement. The restoration of native salmonid fish, in particular bull trout, is a principal focus of the agreement. The result is a collaborative bull trout recovery program with the U.S. Fish and Wildlife Service, Native American tribes and the states of Idaho and Montana on the lower Clark Fork River, consistent with requirements of the FERC license.

The issue of high levels of dissolved gas which exceed Idaho and federal water quality standards downstream of the Cabinet Gorge Hydroelectric Generating Project (Cabinet Gorge) during spill periods continues to be studied, as agreed to in the Clark Fork Settlement Agreement and incorporated into the recently renewed FERC license. To date, intensive biological studies in the lower Clark Fork River and Lake Pend Oreille have documented minimal biological effects of high dissolved gas levels on free ranging fish. Under the terms of the Clark Fork Settlement Agreement, the Company developed an abatement and mitigation strategy during 2002 with the other signatories to the agreement. In December 2002, the Company submitted its plan for review and approval by the other signatories as well as the FERC. The structural alternative proposed in the plan provides for the modification of the two existing diversion tunnels built when Cabinet Gorge was originally constructed. The costs of modifications to the first tunnel are currently estimated to be $37 million (including AFUDC and inflation) and would be incurred between 2004 and 2009. The second tunnel would be modified only after evaluation of the performance of the first tunnel and such modifications would commence no later than 10 years following the completion of the first tunnel. It is currently estimated that the costs to modify the second tunnel would be $23 million (including AFUDC and inflation). As part of the plan, the Company will also provide $0.5 million annually commencing as early as 2004, as mitigation for aquatic resources that might be adversely affected by high dissolved gas levels. Mitigation funds will continue until the modification of the second tunnel commences or if the second tunnel is not modified to an agreed upon point in time commensurate with the biological effects of high dissolved gas levels. The Company will seek regulatory recovery of the costs for the modification of Cabinet Gorge and the mitigation payments.

See "Note 28 of Notes to Consolidated Financial Statements" for additional information.

Dividends

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

Avista Energy holds a significant portion of cash and cash equivalents reflected on the Consolidated Balance Sheet. Covenants in Avista Energy's credit agreement restrict the amount of cash dividends that can be distributed to Avista Capital and ultimately to Avista Corp. During 2002, in accordance with the modified covenants of its credit agreement, Avista Energy paid $116.4 million in dividends to Avista Capital. In January 2003, Avista Energy paid $2.1 million in dividends to Avista Capital.

Quantitative and Qualitative Disclosures About Market Risk

See "Management's Discussion and Analysis of Financial Condition and Results of Operations: Future Outlook: Business Risk and Risk Management."

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

Avista Corporation

For the Years Ended December 31
Dollars in thousands, except per share amounts

	2002	2001	2000
OPERATING REVENUES	$980,446	$1,395,313	$1,858,516
OPERATING EXPENSES:			
Resource costs	453,525	849,996	1,246,459
Operations and maintenance	122,920	125,656	129,708
Administrative and general	118,766	119,216	134,912
Depreciation and amortization	73,275	71,981	65,936
Taxes other than income taxes	67,273	59,172	54,608
Restructuring and exit costs	-	-	9,805
Total operating expenses	835,759	1,226,021	1,641,428
INCOME FROM OPERATIONS	144,687	169,292	217,088
OTHER INCOME (EXPENSE):			
Interest expense	(105,336)	(106,480)	(68,255)
Capitalized interest	7,486	10,498	3,359
Net interest expense	(97,850)	(95,982)	(64,896)
Other income - net	17,467	20,681	25,861
Total other income (expense)-net	(80,383)	(75,301)	(39,035)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	64,304	93,991	178,053
INCOME TAXES	29,994	34,386	76,998
INCOME FROM CONTINUING OPERATIONS	34,310	59,605	101,055
DISCONTINUED OPERATIONS (Note 3):			
Income (loss) before asset impairment charges, minority interest and income taxes	2,499	(21,130)	(15,367)
Asset impairment charges	-	(58,417)	-
Minority interest	-	4,319	2,454
Income tax benefit (expense)	(1,354)	27,779	3,537
INCOME (LOSS) FROM DISCONTINUED OPERATIONS	1,145	(47,449)	(9,376)
NET INCOME BEFORE CUMULATIVE EFFECT OF ACCOUNTING CHANGE	35,455	12,156	91,679
CUMULATIVE EFFECT OF ACCOUNTING CHANGE (net of tax) (Note 2)	(4,148)	-	-
NET INCOME	31,307	12,156	91,679
DEDUCT-Preferred stock dividend requirements	2,402	2,432	23,735
INCOME AVAILABLE FOR COMMON STOCK	$ 28,905	$ 9,724	$ 67,944
Weighted-average common shares outstanding (thousands), Basic	47,823	47,417	45,690
EARNINGS PER COMMON SHARE, BASIC (Note 25):			
Earnings per common share from continuing operations	$ 0.67	$ 1.21	$ 1.69
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.21	1.49
Loss per common share from cumulative effect of accounting change	(0.09)	-	-
Total earnings per common share, basic	$ 0.60	$ 0.21	$ 1.49
Weighted-average common shares outstanding (thousands), Diluted	47,874	47,435	46,103
EARNINGS PER COMMON SHARE, DILUTED (Note 25):			
Earnings per common share from continuing operations	$ 0.67	$ 1.20	$ 1.67
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.20	1.47
Loss per common share from cumulative effect of accounting change	(0.09)	-	-
Total earnings per common share, diluted	$ 0.60	$ 0.20	$ 1.47
Dividends paid per common share	$ 0.48	$ 0.48	$ 0.48
NET INCOME	$31,307	$12,156	$91,679
OTHER COMPREHENSIVE INCOME (LOSS):			
Foreign currency translation adjustment	8	(221)	(82)
Unfunded accumulated benefit obligation - net of tax	(18,081)	(740)	-
Unrealized loss on interest rate swap agreements - net of tax	(1,258)	-	-
Unrealized investments gains (losses) - net of tax	(934)	1,585	(475)
TOTAL OTHER COMPREHENSIVE INCOME (LOSS)	(20,265)	624	(557)
COMPREHENSIVE INCOME	$ 11,042	$ 12,780	$ 91,122

The Accompanying Notes are an Integral Part of These Statements.

CONSOLIDATED BALANCE SHEETS

Avista Corporation

As of December 31

Dollars in thousands

	2002	2001
ASSETS:		
CURRENT ASSETS:		
Cash and cash equivalents	$186,369	$171,221
Temporary investments	-	1,872
Accounts and notes receivable-less allowances of $46,909 and $50,211, respectively	321,091	388,083
Energy commodity assets	365,477	477,037
Materials and supplies, fuel stock and natural gas stored	22,047	21,776
Taxes receivable	-	32,348
Prepayments and other current assets	73,633	19,364
Assets held for sale from discontinued operations	105	21,316
Total current assets	968,722	1,133,017
NET UTILITY PROPERTY:		
Utility plant in service	2,370,811	2,277,779
Construction work in progress	17,581	54,964
Total	2,388,392	2,332,743
Less: Accumulated depreciation and amortization	824,688	767,101
Total net utility property	1,563,704	1,565,642
OTHER PROPERTY AND INVESTMENTS:		
Investment in exchange power-net	40,833	43,314
Non-utility properties and investments-net	204,522	230,800
Non-current energy commodity assets	348,309	383,497
Other property and investments-net	12,702	13,620
Total other property and investments	606,366	671,231
DEFERRED CHARGES:		
Regulatory assets for deferred income tax	139,138	149,033
Other regulatory assets	29,735	192,760
Utility energy commodity derivative assets	60,322	1,889
Power and natural gas deferrals	166,782	265,063
Unamortized debt expense	51,128	41,222
Other deferred charges	28,236	17,366
Total deferred charges	475,341	667,333
TOTAL ASSETS	$3,614,133	$4,037,223
LIABILITIES AND CAPITALIZATION:		
CURRENT LIABILITIES:		
Accounts payable	$340,651	$367,899
Energy commodity liabilities	304,781	373,837
Current portion of long-term debt	71,901	1,827
Short-term borrowings	30,000	75,099
Interest accrued	20,307	18,583
Other current liabilities	172,138	84,587
Liabilities of discontinued operations	1,052	6,642
Total current liabilities	940,830	928,474
NON-CURRENT LIABILITIES AND DEFERRED CREDITS:		
Deferred revenue	672	35,824
Non-current energy commodity liabilities	314,204	299,980
Utility energy commodity derivative liabilities	50,058	159,418
Deferred income taxes	454,147	517,428
Other non-current liabilities and deferred credits	105,546	65,321
Total non-current liabilities and deferred credits	924,627	1,077,971
CAPITALIZATION (See Consolidated Statements of Capitalization)	1,748,676	2,030,778
COMMITMENTS AND CONTINGENCIES (See Notes to Consolidated Financial Statements)		
TOTAL LIABILITIES AND CAPITALIZATION	$3,614,133	$4,037,223

The Accompanying Notes are an Integral Part of These Statements.

CONSOLIDATED STATEMENTS OF CAPITALIZATION

Avista Corporation
As of December 31
Dollars in thousands, except per share amounts

	2002	2001
LONG-TERM DEBT:		
First Mortgage Bonds:		
Secured Medium-Term Notes:		
Series A - 6.25% to 7.90% due 2003 through 2023	$ 89,500	$ 104,500
Series B - 6.50% to 7.89% due 2005 through 2010	59,000	59,000
Total secured medium-term notes	148,500	163,500
First Mortgage Bonds - 7.75% due 2007	150,000	150,000
Total first mortgage bonds	298,500	313,500
Unsecured Pollution Control Bonds:		
Colstrip 1999A, due 2032	66,700	66,700
Colstrip 1999B, due 2034	17,000	17,000
6% Series due 2023	4,100	4,100
Total unsecured pollution control bonds	87,800	87,800
Unsecured Notes:		
Unsecured Medium-Term Notes:		
Series A - 7.94% to 8.99% due 2003 through 2007	3,000	13,000
Series B - 6.75% to 8.23% due 2003 through 2023	74,000	79,000
Series C - 5.99% to 8.02% due 2007 through 2028	99,000	109,000
Series D - 9.125% due 2003	-	175,000
Total unsecured medium-term notes	176,000	376,000
Unsecured 9.75% Senior Notes due 2008	341,529	400,000
Total unsecured notes	517,529	776,000
Other long-term debt	967	962
Unamortized debt discount	(2,161)	(2,547)
Total long-term debt	902,635	1,175,715
COMPANY-OBLIGATED MANDATORILY REDEEMABLE PREFERRED TRUST SECURITIES:		
7.875%, Series A, due 2037	60,000	60,000
Floating Rate, Series B, due 2037	40,000	40,000
Total company-obligated mandatorily redeemable preferred trust securities	100,000	100,000
PREFERRED STOCK-CUMULATIVE:		
10,000,000 shares authorized:		
Subject to mandatory redemption:		
$6.95 Series K; 332,500 and 350,000 shares outstanding ($100 stated value)	33,250	35,000
COMMON EQUITY:		
Common stock, no par value; 200,000,000 shares authorized; 48,044,208 and 47,632,678 shares outstanding	623,092	617,737
Note receivable from employee stock ownership plan	(4,146)	(5,679)
Capital stock expense and other paid in capital	(11,928)	(11,924)
Accumulated other comprehensive loss	(20,364)	(99)
Retained earnings	126,137	120,028
Total common equity	712,791	720,063
TOTAL CAPITALIZATION	$1,748,676	$2,030,778

The Accompanying Notes are an Integral Part of These Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash and Cash Equivalents

Avista Corporation

For the Years Ended December 31

Dollars in thousands

	2002	2001	2000
CONTINUING OPERATING ACTIVITIES:			
Net income	$ 31,307	$ 12,156	$ 91,679
Loss (income) from discontinued operations	(1,145)	47,449	9,376
Cumulative effect of accounting change	4,148	-	-
Non-cash items included in net income:			
Depreciation and amortization	73,275	71,981	65,936
Provision for deferred income taxes	(40,287)	79,141	79,274
Power and natural gas cost amortizations (deferrals), net	68,481	(210,540)	(70,250)
Amortization of debt expense	8,861	5,639	3,409
Impairment of non-operating assets	-	8,240	-
Energy commodity assets and liabilities	87,403	30,238	(174,680)
Other	(10,763)	(12,096)	(32,470)
Changes in working capital components:			
Sale of customer accounts receivable-net	(10,000)	(5,000)	35,000
Accounts and notes receivable	80,203	457,924	(338,512)
Materials and supplies, fuel stock and natural gas stored	(271)	(853)	7,037
Other current assets	(21,921)	15,058	(45,271)
Accounts payable	(27,248)	(518,369)	363,790
Other current liabilities	89,275	(57,038)	89,772
NET CASH PROVIDED BY (USED IN) CONTINUING OPERATING ACTIVITIES	331,318	(76,070)	84,090
CONTINUING INVESTING ACTIVITIES:			
Utility property construction expenditures (excluding AFUDC)	(64,207)	(119,905)	(98,680)
Other capital expenditures	(19,390)	(162,279)	(73,515)
Changes in other property and investments	1,438	10,163	2,106
Repayments received on notes receivable	33,752	1,000	1,297
Proceeds from property sales and sale of subsidiary investments	586	75,953	105,228
Assets acquired and investments in subsidiaries	(461)	(23,321)	(1,496)
NET CASH USED IN CONTINUING INVESTING ACTIVITIES	(48,282)	(218,389)	(65,060)
CONTINUING FINANCING ACTIVITIES:			
Increase (decrease) in short-term borrowings	(45,099)	(88,061)	42,126
Redemption of preferred trust securities	-	-	(10,000)
Proceeds from issuance of long-term debt	621	550,457	224,000
Redemption and maturity of long-term debt	(204,014)	(140,208)	(54,283)
Redemption of preferred stock	(1,750)	-	-
Issuance of common stock	7,035	8,267	4,532
Repurchase of common stock	-	-	(1,907)
Cash dividends paid	(25,456)	(25,110)	(28,304)
Premiums paid for the redemption of long-term debt	(9,456)	-	-
Long-term debt and short-term borrowing issuance costs	(6,534)	(19,693)	(850)
NET CASH PROVIDED BY (USED IN) CONTINUING FINANCING ACTIVITIES	(284,653)	285,652	175,314
NET CASH PROVIDED BY (USED IN) CONTINUING OPERATIONS	(1,617)	(8,807)	194,344
NET CASH PROVIDED BY (USED IN) DISCONTINUED OPERATIONS	16,765	(17,210)	(37,094)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	15,148	(26,017)	157,250
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	171,221	197,238	39,988
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 186,369	$ 171,221	$ 197,238
SUPPLEMENTAL CASH FLOW INFORMATION:			
Cash paid (received) during the period:			
Interest	$ 95,801	$ 98,571	$ 61,774
Income taxes	7,428	(35,874)	(6,855)
Non-cash financing and investing activities:			
Accounts receivable from sale of non-operating assets	-	22,665	-
Series L preferred stock converted to common stock	-	-	271,286
Unrealized loss on interest rate swap agreements	(1,936)	-	-
Unrealized investment gains (losses)	(1,436)	2,437	(475)
Intangible asset related to pension plan	6,366	-	-
Unfunded accumulated benefit obligation	(34,164)	(1,139)	3,500

The Accompanying Notes are an Integral Part of These Statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Avista Corporation

For the Years Ended December 31

Dollars in thousands

	Preferred Stock Series K		Convertible Preferred Stock, Series L		Common Stock		Note Receivable from Employee Stock	Capital Stock Expense and Other	Accumulated Other Comprehensive	Retained	
	Shares	Amount	Shares	Amount	Shares	Amount	Ownership Plan	Paid-in Capital	Income (Loss)	Earnings	Total
Balance as of December 31, 1999	350,000	$35,000	1,508,210	$ 263,309	35,648,239	$318,731	$ (8,240)	$ (4,347)	$ (166)	$ 87,521	$691,808
Net income										91,679	91,679
Conversion of convertible preferred stock into common stock			(1,508,210)	(263,309)	11,410,047	289,118		(8,009)		(17,868)	(68)
Repurchase of common stock					(45,975)	(1,488)				(419)	(1,907)
Stock issued under compensatory plans					70,742	1,192		689		101	1,982
Employee Investment Plan (401-K)					97,478	2,614		(29)			2,585
Dividend Reinvestment Plan					28,158	574					574
Repayments of note receivable							1,200				1,200
Foreign currency translation adjustment									(82)		(82)
Unrealized investment loss-net									(475)		(475)
Cash dividends paid (common stock)										(22,616)	(22,616)
Cash dividends paid (preferred stock)										(5,600)	(5,600)
ESOP dividend tax savings										144	144
Balance as of December 31, 2000	350,000	$35,000	-	$ -	47,208,689	$610,741	$ (7,040)	$ (11,696)	$ (723)	$ 132,942	$759,224
Net income										12,156	12,156
Stock issued under compensatory plans					91,128	1,763		(228)		(14)	1,521
Employee Investment Plan (401-K)					172,681	2,823					2,823
Dividend Reinvestment Plan					160,180	2,410					2,410
Repayments of note receivable							1,361				1,361
Foreign currency translation adjustment									(221)		(221)
Unfunded accumulated benefit obligation									(740)		(740)
Unrealized investment gain-net									1,585		1,585
Cash dividends paid (common stock)										(22,765)	(22,765)
Cash dividends paid (preferred stock)										(2,432)	(2,432)
ESOP dividend tax savings										141	141
Balance as of December 31, 2001	350,000	$35,000	-	$ -	47,632,678	$617,737	$ (5,679)	$ (11,924)	$ (99)	$ 120,028	$755,063
Net income										31,307	31,307
Stock issued under compensatory plans					2,730	74		(4)			70
Employee Investment Plan (401-K)					227,585	3,046					3,046
Dividend Reinvestment Plan					181,215	2,235					2,235
Redemption of preferred stock	(17,500)	(1,750)									(1,750)
Repayments of note receivable							1,533				1,533
Foreign currency translation adjustment									8		8
Unfunded accumulated benefit obligation									(18,081)		(18,081)
Unrealized investment gain-net									(934)		(934)
Unrealized loss on interest rate swap									(1,258)		(1,258)
Cash dividends paid (common stock)										(22,955)	(22,955)
Cash dividends paid (preferred stock)										(2,402)	(2,402)
ESOP dividend tax savings										159	159
Balance as of December 31, 2002	332,500	$33,250	-	$ -	48,044,208	$623,092	$ (4,146)	$ (11,928)	$ (20,364)	$ 126,137	$746,041

The Accompanying Notes are an Integral Part of These Statements.

SCHEDULE OF INFORMATION BY BUSINESS SEGMENTS

Avista Corporation

For the Years Ended December 31

Dollars in thousands

	2002	2001	2000
OPERATING REVENUES:			
Avista Utilities	$893,964	$1,230,847	$1,512,101
Energy Trading and Marketing (net margin on trading activities)	54,207	134,266	307,746
Information and Technology	17,630	13,815	5,732
Other	14,645	16,385	32,937
Total operating revenues	$980,446	$1,395,313	$1,858,516
RESOURCE COSTS (AVISTA UTILITIES):			
Avista Utilities:			
Power purchased	$ 115,282	$ 708,321	$ 1,072,475
Natural gas purchased	170,662	220,692	169,924
Fuel for generation	18,531	81,949	69,077
Power and natural gas cost amortizations (deferrals), net	68,481	(210,540)	(70,250)
Other fuel costs	77,885	43,269	1,187
Other regulatory amortizations, net	(15,157)	(19,494)	(10,525)
Other resource costs	17,841	25,799	14,571
Total resource costs (Avista Utilities)	$453,525	$849,996	$1,246,459
AVISTA UTILITIES GROSS MARGIN:	$440,439	$380,851	$265,642
OPERATIONS AND MAINTENANCE EXPENSES:			
Avista Utilities	$97,668	$97,831	$95,117
Energy Trading and Marketing	-	-	249
Information and Technology	10,559	12,607	6,611
Other	14,693	15,218	27,731
Total operations and maintenance expenses	$122,920	$125,656	$129,708
ADMINISTRATIVE AND GENERAL EXPENSES:			
Avista Utilities	$63,751	$53,416	$62,111
Energy Trading and Marketing	21,820	33,494	41,256
Information and Technology	19,855	23,918	22,329
Other	13,340	8,388	9,216
Total administrative and general expenses	$118,766	$119,216	$134,912
DEPRECIATION AND AMORTIZATION EXPENSES:			
Avista Utilities	$66,243	$61,383	$57,479
Energy Trading and Marketing	1,227	2,188	2,466
Information and Technology	4,376	5,403	2,169
Other	1,429	3,007	3,822
Total depreciation and amortization expenses	$73,275	$71,981	$65,936
INCOME FROM OPERATIONS (PRE-TAX):			
Avista Utilities	$149,180	$114,927	$3,177
Energy Trading and Marketing	29,211	94,669	250,196
Information and Technology	(18,818)	(29,872)	(26,424)
Other	(14,886)	(10,432)	(9,861)
Total income from operations	$144,687	$169,292	$217,088
INCOME FROM CONTINUING OPERATIONS:			
Avista Utilities	$36,382	$24,164	$(38,781)
Energy Trading and Marketing	22,425	63,246	161,753
Information and Technology	(12,117)	(19,384)	(19,032)
Other	(12,380)	(8,421)	(2,885)
Total income from continuing operations	$34,310	$59,605	$101,055
ASSETS:			
Avista Utilities	$2,184,008	$2,396,317	$2,143,791
Energy Trading and Marketing	1,349,626	1,506,185	10,271,834
Information and Technology	37,528	26,891	14,429
Other	42,866	86,514	96,362
Discontinued Operations	105	21,316	50,665
Total assets	$3,614,133	$4,037,223	$12,577,081
CAPITAL EXPENDITURES:			
Avista Utilities	$64,207	$119,905	$98,680
Energy Trading and Marketing	17,531	157,020	65,095
Information and Technology	1,626	4,644	8,409
Other	233	615	976
Total capital expenditures	$83,597	$282,184	$173,160

The Accompanying Notes are an Integral Part of These Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business
Avista Corporation (Avista Corp. or the Company) is an energy company engaged in the generation, transmission and distribution of energy as well as other energy-related businesses. The utility portion of the Company, doing business as Avista Utilities, an operating division of Avista Corp. and not a separate entity, represents the regulated utility operations. Avista Utilities provides electric and natural gas distribution and transmission services in eastern Washington and northern Idaho. Avista Utilities also provides natural gas distribution service in northeast and southwest Oregon and in the South Lake Tahoe region of California. Avista Capital, a wholly owned subsidiary of Avista Corp., is the parent company of all of the subsidiary companies engaged in the other non-utility lines of business.

The Company's operations are exposed to risks including, but not limited to, the effects of legislative and governmental regulations, the price and supply of purchased power, fuel and natural gas, recoverability of power and natural gas costs, streamflow and weather conditions, availability of generation facilities, competition, technology and availability of funding. In addition, the energy business exposes the Company to the financial, liquidity, credit and commodity price risks associated with wholesale purchases and sales.

Basis of Reporting
The consolidated financial statements include the assets, liabilities, revenues and expenses of the Company and its subsidiaries. The accompanying financial statements include the Company's proportionate share of utility plant and related operations resulting from its interests in jointly owned plants (See Note 10).

Use of Estimates
The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the consolidated financial statements and thus actual results could differ from the amounts reported and disclosed herein.

System of Accounts
The accounting records of the Company's utility operations are maintained in accordance with the uniform system of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and adopted by the appropriate state regulatory commissions.

Regulation
The Company is subject to state regulation in Washington, Idaho, Montana, Oregon and California. The Company is subject to federal regulation by the FERC.

Business Segments
Financial information for each of the Company's lines of business is reported in the Schedule of Information by Business Segments. Such information is an integral part of these consolidated financial statements. The business segment presentation reflects the basis currently used by the Company's management to analyze performance and determine the allocation of resources. Avista Utilities' business is managed based on the total regulated utility operation. The Energy Trading and Marketing line of business operations primarily include non-regulated electricity and natural gas marketing and trading activities including derivative commodity instruments such as futures, options, swaps and other contractual arrangements. The Information and Technology line of business operations includes utility internet billing services and fuel cell technology. The Other line of business includes other investments and operations of various subsidiaries as well as the operations of Avista Capital on a parent company only basis.

Avista Utilities Operating Revenues
Operating revenues for Avista Utilities related to the sale of energy are generally recorded when service is rendered or energy is delivered to customers. The determination of the energy sales to individual customers is based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each month, the amount of energy delivered to customers since the date of the last meter reading is estimated and the corresponding unbilled revenue is estimated and recorded. Accounts receivable includes unbilled energy revenues of $6.1 million

(net of $40.9 million of unbilled receivables sold) and $11.1 million (net of $46.6 million of unbilled receivables sold) as of December 31, 2002 and 2001, respectively. See Note 6 for information with respect to the sale of accounts receivable.

Avista Energy Operating Revenues

Avista Energy followed the mark-to-market method of accounting for energy contracts entered into for trading and price risk management purposes in compliance with Emerging Issues Task Force (EITF) Issue No. 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities" through December 31, 2002 for contracts entered into on or prior to October 25, 2002. Avista Energy recognized revenue based on the change in the market value of outstanding derivative commodity sales contracts, net of future servicing costs and reserves, in addition to revenue related to settled contracts. For all contracts entered into subsequent to October 25, 2002 and for all contracts beginning January 1, 2003, Avista Energy follows Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." See Note 2 for a discussion of the rescission of EITF Issue No. 98-10 in October 2002.

Research and Development Expenses

Company-sponsored research and development expenditures are expensed as incurred. The majority of the Company's research and development expenses are related to the Information and Technology line of business. Research and development expenses totaled $3.8 million, $8.4 million and $8.1 million in 2002, 2001 and 2000, respectively.

Advertising Expenses

The Company expenses advertising costs as incurred. Advertising expenses totaled $1.3 million, $1.8 million and $1.2 million in 2002, 2001 and 2000, respectively.

Taxes other than income taxes

Taxes other than income taxes include state excise taxes, city occupational and franchise taxes, real and personal property taxes and certain other taxes not based on net income. These taxes are generally based on revenues or the value of property. Utility related taxes collected from customers are recorded as both operating revenue and expense and totaled $33.1 million, $26.3 million and $23.5 million in 2002, 2001 and 2000, respectively.

Other Income-Net

Other income-net consisted of the following items for the years ended December 31 (dollars in thousands):

	2002	2001	2000
Interest income	$ 7,716	$19,049	$10,351
Interest on power and natural gas deferrals	9,597	12,995	1,473
Impairment of non-operating assets	-	(8,240)	-
Net gain (loss) on the disposition of assets	(33)	2,884	21,048
Minority interest	242	217	694
Other expense	(8,064)	(10,839)	(10,234)
Other income	8,009	4,615	2,529
Total	$17,467	$20,681	$25,861

Income Taxes

The Company and its eligible subsidiaries file consolidated federal income tax returns. Subsidiaries are charged or credited with the tax effects of their operations on a stand-alone basis. The Company's federal income tax returns were examined with all issues resolved, and all payments made, through the 1998 return.

The Company accounts for income taxes using the liability method. Under the liability method, a deferred tax asset or liability is determined based on the enacted tax rates that will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in the Company's consolidated income tax returns. The deferred tax expense for the period is equal to the net change in the deferred tax asset and liability accounts from the beginning to the end of the period. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

Stock-Based Compensation
The Company follows the disclosure only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." Accordingly, employee stock options are accounted for under Accounting Principle Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees." Stock options are granted at exercise prices not less than the fair value of common stock on the date of grant. Under APB No. 25, no compensation expense is recognized pursuant to the Company's stock option plans.

If compensation expense for the Company's stock option plans were determined consistent with SFAS No. 123, net income and earnings per common share would have been the following pro forma amounts for the years ended December 31:

	2002	2001	2000
Net income (dollars in thousands):			
As reported	$31,307	$12,156	$91,679
Pro forma	$28,256	$ 9,355	$89,850
Basic earnings per common share			
As reported	$0.60	$0.21	$1.49
Pro forma	$0.54	$0.15	$1.45
Diluted earnings per common share			
As reported	$0.60	$0.20	$1.47
Pro forma	$0.54	$0.15	$1.43

Comprehensive Income
The Company's comprehensive income is comprised of net income, foreign currency translation adjustments, unfunded accumulated benefit obligation, unrealized gains and losses on interest rate swap agreements and unrealized gains and losses on investments available-for-sale.

Foreign Currency Translation Adjustment
The assets and liabilities of Avista Energy Canada, Ltd. and its subsidiary, Copac Management, Inc. are denominated in Canadian dollars and translated to United States dollars at exchange rates in effect on the balance sheet date. Revenues and expenses are translated using an average exchange rate. Translation adjustments resulting from this process are reflected as a component of other comprehensive income in the Consolidated Statements of Comprehensive Income.

Earnings Per Common Share
Basic earnings per common share is computed by dividing income available for common stock by the weighted average number of common shares outstanding for the period. Diluted earnings per common share is calculated by dividing income available for common stock by diluted weighted average common shares outstanding during the period, including common stock equivalent shares outstanding using the treasury stock method, unless such shares are anti-dilutive. Common stock equivalent shares include shares issuable upon exercise of stock options and convertible stock. See Note 25 for earnings per common share calculations.

Cash and Cash Equivalents
For the purposes of the Consolidated Statements of Cash Flows, the Company considers all temporary investments with a purchased maturity of three months or less to be cash equivalents. Cash and cash equivalents include cash deposits from counterparties. See Note 9 for further information with respect to cash deposits from counterparties.

Temporary Investments
Temporary investments consist of marketable equity securities classified as "available for sale." The Company did not have any temporary investments in marketable equity securities as of December 31, 2002. The unrealized gain on temporary investments totaled $1.4 million as of December 31, 2001, net of taxes, and is reflected as a component of accumulated other comprehensive income in the Consolidated Statements of Capitalization.

Allowance for Doubtful Accounts
The Company maintains an allowance for doubtful accounts to sufficiently provide for estimated and potential losses on accounts receivable. The Company determines the allowance for utility and other customer accounts receivable based on historical write-offs as compared to accounts receivable and operating revenues. Additionally, the Company establishes specific allowances for certain individual accounts.

The following table documents the activity in the allowance for doubtful accounts during the years ended December 31 (dollars in thousands):

	2002	2001	2000
Allowance as of the beginning of the year	$50,211	$14,404	$ 4,267
Additions expensed during the year	3,469	39,947	11,835
Net deductions	(6,771)	(4,140)	(1,698)
Allowance as of the end of the year	$46,909	$50,211	$14,404

Inventory
Inventory consists primarily of materials and supplies, fuel stock and natural gas stored. Inventory is recorded at the lower of cost or market, primarily using the average cost method.

Utility Plant in Service
The cost of additions to utility plant in service, including an allowance for funds used during construction and replacements of units of property and improvements, is capitalized. Costs of depreciable units of property retired plus costs of removal less salvage are charged to accumulated depreciation.

Allowance for Funds Used During Construction
The Allowance for Funds Used During Construction (AFUDC) represents the cost of both the debt and equity funds used to finance utility plant additions during the construction period. In accordance with the uniform system of accounts prescribed by regulatory authorities, AFUDC is capitalized as a part of the cost of utility plant and is credited currently as a non-cash item in the Consolidated Statements of Income and Comprehensive Income in the line item capitalized interest. The Company generally is permitted, under established regulatory rate practices, to recover the capitalized AFUDC, and a fair return thereon, through its inclusion in rate base and the provision for depreciation after the related utility plant is placed in service. Cash inflow related to AFUDC does not occur until the related utility plant is placed in service.

The effective AFUDC rate was 9.72 percent for the second half of 2002, 9.03 percent for the first half of 2002 and 2001, and 10.67 percent in 2000. The Company's AFUDC rates do not exceed the maximum allowable rates as determined in accordance with the requirements of regulatory authorities.

Depreciation
For utility operations, depreciation expense is estimated by a method of depreciation accounting utilizing unit rates for hydroelectric plants and composite rates for other utility plant. Such rates are designed to provide for retirements of properties at the expiration of their service lives. The rates for hydroelectric plants include annuity and interest components, in which the interest component is 9 percent. For utility operations, the ratio of depreciation provisions to average depreciable property was 2.92 percent in 2002, 2.84 percent in 2001 and 2.72 percent in 2000.

The average service lives and remaining average service lives, respectively, for the following broad categories of utility property are: electric thermal production - 35 and 14 years; hydroelectric production - 100 and 76 years; electric transmission - 60 and 25 years; electric distribution - 40 and 28 years; and natural gas distribution property - 44 and 27 years.

Goodwill
Goodwill arising from acquisitions represents the excess of the purchase price over the estimated fair value of net assets acquired. The Company evaluates goodwill for impairment on at least an annual basis. Goodwill is included in non-utility properties and investments-net in the Consolidated Balance Sheets and totaled $7.3 million and $13.7 million as of December 31, 2002 and 2001, respectively. The level of goodwill as of December 31, 2002 and 2001 was supported by the value attributed to the operations acquired. See Note 2 for changes in accounting for goodwill effective January 1, 2002.

Regulatory Deferred Charges and Credits
The Company prepares its consolidated financial statements in accordance with the provisions of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation." The Company prepares its financial statements in accordance with SFAS No. 71 because (i) the Company's rates for regulated services are established by or subject to approval by an independent third-party regulator, (ii) the regulated rates are designed to recover the Company's cost of providing the regulated services and (iii) in view of demand for the regulated services and the level of

competition, it is reasonable to assume that rates can be charged to and collected from customers at levels that will recover the Company's costs. SFAS No. 71 requires the Company to reflect the impact of regulatory decisions in its financial statements. SFAS No. 71 requires that certain costs and/or obligations (such as incurred power and natural gas costs not currently recovered through rates, but expected to be recovered in the future) are reflected as deferred charges on the balance sheet. These costs and/or obligations are not reflected in the statement of income until the period during which matching revenues are recognized. If at some point in the future the Company determines that it no longer meets the criteria for continued application of SFAS No. 71 with respect to all or a portion of the Company's regulated operations, the Company could be required to write off its regulatory assets. The Company could also be precluded from the future deferral of costs not recovered through rates at the time such costs were incurred, even if such costs were expected to be recovered in the future.

The Company's primary regulatory assets include power and natural gas deferrals (see "Power Cost Deferrals" and "Natural Gas Cost Deferrals" below for further information), investment in exchange power (see "Investment in Exchange Power-Net" below for further information), regulatory assets for deferred income taxes (see Note 13 for further information), unamortized debt expense (see "Unamortized Debt Expense" below for further information), regulatory asset offsetting energy commodity derivative liabilities (see Note 7 for further information), demand side management programs, conservation programs and the provision for postretirement benefits. Those items without a specific line on the Consolidated Balance Sheets are included in other regulatory assets. Other regulatory assets consisted of the following as of December 31 (dollars in thousands):

	2002	2001
Regulatory asset offsetting energy commodity derivative liabilities......	$ -	$157,529
Regulatory asset for postretirement benefit obligation..........................	4,728	5,200
Demand side management and conservation programs.........................	23,733	28,813
Other..	1,274	1,218
Total..	$29,735	$192,760

Deferred credits include, among other items, regulatory liabilities created when the Centralia Power Plant (Centralia) was sold and the gain on the general office building sale/leaseback which is being amortized over the life of the lease, and are included on the Consolidated Balance Sheets as other non-current liabilities and deferred credits.

Investment in Exchange Power-Net

The investment in exchange power represents the Company's previous investment in Washington Public Power Supply System Project 3 (WNP-3), a nuclear project that was terminated prior to completion. Under a settlement agreement with the Bonneville Power Administration in 1985, Avista Utilities began receiving power in 1987, for a 32.5-year period, related to its investment in WNP-3. Through a settlement agreement with the Washington Utilities and Transportation Commission (WUTC) in the Washington jurisdiction, Avista Utilities is amortizing the recoverable portion of its investment in WNP-3 (recorded as investment in exchange power) over a 32.5 year period beginning in 1987. For the Idaho jurisdiction, Avista Utilities has fully amortized the recoverable portion of its investment in exchange power.

Unamortized Debt Expense

Unamortized debt expense includes debt issuance costs that are amortized over the life of the related debt, as well as premiums paid to repurchase debt, which are amortized over the average remaining maturity of outstanding debt in accordance with regulatory accounting practices under SFAS No. 71.

Natural Gas Benchmark Mechanism

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

The Natural Gas Benchmark Mechanism provides benefits to retail customers and allows Avista Energy to retain a portion of the benefits associated with asset optimization and the efficiencies gained in purchasing natural gas for Avista Utilities. In the first quarter of 2002, the IPUC and the OPUC approved the continuation of the Natural Gas

Benchmark Mechanism and related Agency Agreement through March 31, 2005. In January 2003, the WUTC approved the continuation of the Natural Gas Benchmark Mechanism and related Agency Agreement through January 29, 2004. Hearings will be held before the WUTC during 2003 to determine whether or not the Natural Gas Benchmark Mechanism and related Agency Agreement will be extended beyond January 29, 2004.

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

Avista Utilities' natural gas purchases from Avista Energy totaled $114.8 million, $249.8 million and $175.9 million in 2002, 2001 and 2000, respectively. These costs are reflected as resource costs in the Consolidated Statements of Income and Comprehensive Income.

Power Cost Deferrals

Avista Utilities defers the recognition in the income statement of certain power supply costs as approved by the WUTC. Deferred power supply costs are recorded as a deferred charge on the balance sheet for future review and the opportunity for recovery through retail rates. The power supply costs deferred include certain differences between actual power supply costs incurred by Avista Utilities and the costs included in base retail rates. This difference in power supply costs primarily results from changes in short-term wholesale market prices, changes in the level of hydroelectric generation and changes in the level of thermal generation (including changes in fuel prices). Avista Utilities accrues interest on deferred power costs in the Washington jurisdiction at a rate, which is adjusted semi-annually, of 8.9 percent as of December 31, 2002. Total deferred power costs for Washington customers were $123.7 million and $140.2 million as of December 31, 2002 and 2001, respectively.

In June 2002, the WUTC issued an order that became effective July 1, 2002. The order provides for an overall rate of return of 9.72 percent and a return on equity of 11.16 percent. The order provided for no incremental rate increase to Avista Utilities' Washington electric customers above the rates in effect at that time. Rate increases previously approved by the WUTC totaling 31.2 percent (a 25 percent temporary surcharge approved in September 2001 for the recovery of deferred power costs and a 6.2 percent increase approved in March 2002) were restructured. The general increase to base retail rates was 19.3 percent (or $45.7 million in annual revenues) and the remaining 11.9 percent represents the continued recovery of deferred power costs over a period currently projected to continue into 2009.

In the June 2002 rate order, the WUTC approved the establishment of an Energy Recovery Mechanism (ERM). The ERM replaced a series of temporary deferral mechanisms that were in place in Washington since mid-2000. The ERM allows Avista Utilities to increase or decrease electric rates periodically with WUTC approval to reflect changes in power supply costs. The ERM provides for Avista Utilities to incur the cost of, or receive the benefit from, the first $9 million in annual power supply costs above or below the amount included in base retail rates. As the ERM was implemented on July 1, 2002, the Company's expense or benefit was limited to $4.5 million for 2002. Under the ERM, 90 percent of annual power supply costs exceeding or below the initial $9 million ($4.5 million for 2002) will be deferred for future surcharge or rebate to Avista Utilities' customers. The remaining 10 percent will be an expense of, or benefit to, the Company.

Avista Utilities has a power cost adjustment (PCA) mechanism in Idaho that allows it to modify electric rates periodically with IPUC approval to recover or rebate a portion of the difference between actual and allowed net power supply costs. The PCA mechanism allows for the deferral of 90 percent of the difference between actual net power supply expenses and the authorized level of net power supply expenses approved in the last Idaho general rate case. Avista Utilities accrues interest on deferred power costs in the Idaho jurisdiction at a rate, which is adjusted annually, of 2 percent as of December 31, 2002. In October 2002, the IPUC issued an order extending a 19.4 percent PCA surcharge for Idaho electric customers. The PCA surcharge will remain in effect until October 2003. The IPUC directed Avista Utilities to file a status report 60 days before the PCA surcharge expires. If review of the status report and the actual balance of deferred power costs support continuation of the PCA surcharge, the IPUC has indicated that it anticipates the PCA surcharge will be extended for an additional period. Total deferred power costs for Idaho customers were $31.5 million and $73.1 million as of December 31, 2002 and 2001, respectively.

Natural Gas Cost Deferrals
Under established regulatory practices in each respective state, Avista Utilities is allowed to adjust its natural gas rates periodically (with appropriate regulatory approval) to reflect increases or decreases in the cost of natural gas purchased. Differences between actual natural gas costs and the natural gas costs allowed in rates are deferred and charged or credited to expense when regulators approve inclusion of the cost changes in rates. Total deferred natural gas costs were $11.5 million and $52.7 million as of December 31, 2002 and 2001, respectively.

Deferred Revenue
In December 1998, the Company received cash proceeds of $143.4 million from a transaction in which the Company assigned and transferred certain rights under a long-term power sales contract to a funding trust. The proceeds were recorded as deferred revenue and were being amortized into revenues over the 16-year period of the long-term sales contract. Pursuant to the WUTC order in September 2001, the Company was directed to offset $53.8 million of the Washington share of the deferred revenue against deferred power costs. The IPUC order in October 2001 directed the Company to amortize the remaining Idaho share ($34.6 million) of the deferred revenue against deferred power costs over the 15-month period between October 2001 and December 2002. The balance was fully amortized as of December 31, 2002.

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

NOTE 2. NEW ACCOUNTING STANDARDS

In June 2001, the Financial Accounting Standards Board (FASB) issued SFAS No. 142, "Goodwill and Other Intangible Assets" which applies to acquired intangible assets whether acquired singly, as part of a group, or in a business combination. This statement requires that goodwill not be amortized; however, goodwill for each reporting unit must be evaluated for impairment on at least an annual basis using a two-step approach. The first step used to identify potential impairment compares the estimated fair value of a reporting unit to its carrying amount, including goodwill. If the fair value of a reporting unit is less than its carrying amount, the second step of the impairment evaluation, which compares the implied fair value of goodwill to its carrying amount, is performed to determine the amount of the impairment loss, if any. This statement also provides standards for financial statement disclosures of goodwill and other intangible assets and related impairment losses. The Company adopted this statement on January 1, 2002.

In April 2002, the Company completed its transitional test of goodwill. Accordingly, the Company determined that goodwill related to Advanced Manufacturing and Development, a subsidiary of Avista Ventures included in the Other business segment, was impaired. This was due to a change in forecasted earnings based on the decline in the performance of the business. The fair value of the reporting unit was determined using the present value of projected future cash flows. The Company recorded an impairment of $4.1 million, net of taxes, as a cumulative effect of accounting change in the Consolidated Statement of Income and Comprehensive Income.

Goodwill amortization was $1.8 million, net of taxes, for 2001. Net income and basic and diluted earnings per common share would have been $14.0 million, $0.24 and $0.24, respectively, excluding goodwill amortization for 2001. Goodwill amortization was $2.2 million, net of taxes, for 2000. Net income and basic and diluted earnings per common share would have been $93.9 million, $1.54 and $1.52, respectively, excluding goodwill amortization for 2000.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations" which addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This statement requires the recording of the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the associated costs of the asset retirement obligation will be capitalized as part of the carrying amount of the related long-lived asset. The liability will be accreted to its present value each period and the related capitalized costs will be depreciated over the useful life of the related asset. Upon retirement of the asset, the Company will either settle the retirement obligation for its recorded amount or incur a gain or loss. The adoption of this statement on January 1, 2003 did not have a material impact on the Company's financial condition or results of operations. The Company recovers certain asset retirement costs through rates charged to customers as a portion of its depreciation expense. As of December 31, 2002, the Company had estimated retirement costs of $185.4 million included in accumulated depreciation.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" which nullifies EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." This statement requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred. Under EITF Issue No. 94-3, a liability for an exit cost was recognized at the date of an entity's commitment to an exit plan. This statement also requires the initial measurement of the liability at fair value. This statement is effective for exit or disposal activities that are initiated after December 31, 2002. The adoption of this statement did not have any impact on the Company's financial condition or results of operations.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure" which amends SFAS No. 123 "Accounting for Stock-Based Compensation." This statement provides alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based compensation. In addition, this statement requires the disclosure of pro forma net income and earnings per common share had the Company adopted the fair value method of accounting for stock-based compensation in a more prominent place in the financial statements (Note 1). This statement also requires the disclosure of pro forma net income and earnings per common share in interim as well as annual financial statements. The alternative transition methods and annual financial statement disclosures are effective for fiscal years ending after December 15, 2002. Interim disclosures are required for periods ending after December 15, 2002. The adoption of this statement affects the Company's disclosures. As the Company has not elected to adopt the fair value method of accounting for stock-based compensation, the adoption of this statement does not have any impact on the Company's financial condition or results of operations.

In June 2002, the EITF reached a partial consensus on Issue No. 02-3 regarding the accounting for contracts involved in energy trading and risk management activities. The partial consensus required that all gains and losses arising from energy trading contracts (whether realized or unrealized) accounted for under EITF Issue No. 98-10 were to be presented on a net basis in the income statement beginning in the third quarter of 2002. Reclassification of all historical comparable periods was required. This applied to the activities of Avista Energy; Avista Utilities does not have energy trading contracts that were accounted for under EITF Issue No. 98-10. Avista Energy historically presented unrealized gains and losses on energy trading contracts on a net basis. However, realized contracts were presented on a gross basis for both operating revenues and resource costs. The implementation of EITF Issue 02-3 resulted in reduced operating revenues and resource costs as compared to historical periods with no impact on the Company's net income or financial condition.

Avista Energy accounted for energy commodity trading activity in compliance with EITF Issue No. 98-10 through December 31, 2002 for contracts entered into on or prior to October 25, 2002. Under EITF 98-10, Avista Energy recognized revenue based on the change in the market value of outstanding derivative commodity sales contracts, net of future servicing costs and reserves, in addition to revenue related to settled contracts. In October 2002, the EITF rescinded Issue No. 98-10. As such, Avista Energy is required to account for energy trading contracts that meet the definition of a derivative at market value in compliance with SFAS No. 133. This applies to all existing contracts as of January 1, 2003 as well as to all new contracts entered into subsequent to October 25, 2002. Contracts not meeting the definition of a derivative are no longer accounted for at market value and include Avista Energy's Agency Agreement with Avista Utilities, natural gas storage contracts, tolling agreements and natural gas transportation agreements. The transition from EITF Issue No. 98-10 to accrual based accounting resulted in the adjustment of the contracts that are not considered derivatives from their market value to their cost basis. Any gain or loss on contracts that are not considered derivatives will not be recognized until the contract is settled or realized. The Company anticipates that the changes will primarily affect the timing of the recognition of income or loss in earnings, and not change the underlying economics or cash flows of transactions entered into by Avista Energy. The changes could result in a significant increase in the volatility of reported earnings on a quarter-to-quarter and year-to-year basis. On January 1, 2003, Avista Energy recorded as a cumulative effect of accounting change a charge of approximately $1.2 million (net of tax) related to the transition from EITF 98-10 to SFAS No. 133.

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." This interpretation clarifies the requirements of SFAS No. 5, "Accounting for Contingencies" relating to a guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. This interpretation requires that upon issuance of a guarantee, the guarantor must recognize a liability for the fair value of the obligation it assumes under that guarantee. The initial recognition and measurement provisions of this interpretation are to be applied on a prospective basis to guarantees issued or modified subsequent to December 31, 2002 and are not expected to have a material impact on the Company's financial condition or results of operations. The disclosure requirements of this interpretation are effective for financial statements issued for periods that end after December 15, 2002. See Note 19 for disclosure of the Company's guarantees.

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

The application of this FASB interpretation will require the Company to consolidate WP Funding LP effective July 1, 2003. WP Funding LP is an entity that was formed for the purpose of acquiring the natural gas-fired combustion turbine generating facility in Rathdrum, Idaho (Rathdrum CT). WP Funding LP purchased the Rathdrum CT from the Company with funds provided by unrelated investors of which 97 percent represented debt and 3 percent represented equity. The Company operates the Rathdrum CT and leases it from WP Funding LP and currently makes lease payments of $4.5 million per year. The total amount of WP Funding LP debt outstanding that is not included on the Company's balance sheet was $54.5 million as of December 31, 2002. The lease term expires in February 2020; however, the current debt matures in October 2005 and will need to be refinanced at that time. Based on current information, the difference between the book value of the debt and equity of WP Funding LP and the book value of the Rathdrum CT is approximately $15.5 million ($10.1 million, net of taxes). The Company intends to request regulatory accounting orders to record this amount as a regulatory asset upon the consolidation of WP Funding LP.

NOTE 3. DISCONTINUED OPERATIONS

In September 2001, the Company reached a decision that it would dispose of substantially all of the assets of Avista Communications. In October 2001, minority shareholders of Avista Communications acquired ownership of its Montana and Wyoming operations as well as its dial-up internet access operations in Spokane, Washington and Coeur d'Alene, Idaho. In December 2001, Avista Communications completed the sale of the assets and customer accounts of its Yakima and Bellingham, Washington operations to Advanced Telcom Group, Inc. In April 2002, Avista Communications completed the transfer of voice and integrated services customer accounts in Spokane, Washington and Lewiston and Coeur d'Alene, Idaho to certain subsidiaries of XO Communications, Inc. In December 2002, the Company completed the sale of substantially all of the remaining assets of Avista Communications to FiberLink LLC. The divestiture of the operating assets of Avista Communications was substantially complete by the end of 2002. Certain liabilities of the operations remain to be settled.

Revenues for Avista Communications were $3.5 million, $11.5 million and $5.9 million in 2002, 2001 and 2000, respectively. Total assets of $21.3 million as of December 31, 2001 were comprised of $16.6 million of deferred tax assets, $3.2 million of fixed assets and $1.5 million of current assets including accounts receivable, cash, inventory and prepaid expenses.

Concurrent with the decision to dispose of Avista Communications, the Company assessed the carrying value of assets and goodwill of Avista Communications. The assets and goodwill of Avista Communications were written down to the estimated fair value based upon the planned disposal of the assets. The total charges of $58.4 million incurred in 2001 were comprised of the following: $48.2 million for asset impairment, $7.1 million for goodwill impairment and $3.1 million for exit costs and other costs to sell Avista Communications.

NOTE 4. IMPAIRMENT OF NON-OPERATING ASSETS

In 2001, the Company recorded an impairment charge related to three turbines owned by Avista Power. The Company originally planned to use the turbines in a non-regulated generation project. Due to changing market conditions the Company decided to no longer pursue the development of additional non-regulated generation projects. The Company wrote down the carrying value of the turbines to estimated fair value less selling costs. This resulted in a charge of $8.2 million for 2001 included in other income-net in the Consolidated Statements of Income and Comprehensive Income.

NOTE 5. RESTRUCTURING AND EXIT COSTS

In November 1999, Avista Energy redirected its focus away from national energy trading toward a more regional-based energy marketing and trading effort in the western United States. The downsizing plan called for the shutting down of operations in Houston and Boston during the first half of 2000 and eliminating approximately 80 positions. In the fourth quarter of 1999, Avista Energy recorded a charge of $9.3 million for expenses related to employee terminations and recorded $33.6 million of goodwill impairment. Avista Energy sold its eastern United States power book during the first quarter of 2000 for a $1.5 million loss, but did not find a buyer for its natural gas or coal contracts in the eastern United States. The remaining eastern United States natural gas contracts, primarily for transportation and storage, were managed out of the Spokane office until the last of the contracts expired in 2002. In addition to the restructuring charges previously reserved and paid, other transition costs of $6.4 million for 2000 were incurred for closing the Houston and Boston offices and phasing out operations in the eastern United States.

In the first quarter of 2000, it was announced that Pentzer would be redirecting its focus. Pentzer recorded a charge of $1.9 million for expenses related to employee terminations, which were paid during 2000.

NOTE 6. ACCOUNTS RECEIVABLE SALE

In 1997, Avista Receivables Corp. (ARC), formerly known as WWP Receivables Corp., was formed as a wholly owned, bankruptcy-remote subsidiary of the Company for the purpose of acquiring or purchasing interests in certain accounts receivable, both billed and unbilled, of the Company. On May 29, 2002, ARC, the Company and a third-party financial institution entered into a three-year agreement whereby ARC can sell without recourse, on a revolving basis, up to $100.0 million of those receivables. ARC is obligated to pay fees that approximate the purchaser's cost of issuing commercial paper equal in value to the interests in receivables sold. On a consolidated basis, the amount of such fees is included in operating expenses of the Company. As of December 31, 2002 and 2001, $65.0 million and $75.0 million, respectively, in accounts receivables were sold.

NOTE 7. UTILITY ENERGY COMMODITY DERIVATIVE ASSETS AND LIABILITIES

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

Avista Utilities enters into forward contracts to purchase or sell energy. Under forward contracts, Avista Utilities commits to purchase or sell a specified amount of energy at a specified time, or during a specified period, in the future. Certain of these forward contracts are considered derivative instruments. Avista Utilities also records derivative commodity assets and liabilities for over-the-counter and exchange-traded derivative instruments as well as certain long-term contracts. These contracts are entered into to manage Avista Utilities' loads and resources as discussed in Note 8. In conjunction with the issuance of SFAS No. 133, the WUTC and the IPUC issued accounting orders requiring Avista Utilities to offset any derivative assets or liabilities with a regulatory asset or liability. This accounting treatment is intended to defer the recognition of mark-to-market gains and losses on energy commodity transactions until the period of settlement. The order provides for Avista Utilities to not recognize the unrealized gain or loss on utility derivative commodity instruments in the Consolidated Statements of Income and Comprehensive Income. Such realized gains or losses are recognized in the period of settlement subject to current or future recovery in retail rates. Avista Energy accounted for derivative commodity instruments using the mark-to-market method of accounting under EITF Issue No. 98-10 through December 31, 2002, which was rescinded in October 2002 as discussed in Note 2. See Note 8 for details of Avista Energy's disclosures of derivative commodity instruments.

Avista Utilities believes substantially all of its purchases and sales contracts for both capacity and energy qualify as normal purchases and sales under SFAS No. 133 and are not required to be recorded as derivative commodity assets and liabilities. Contracts that are not considered derivatives under SFAS No. 133 are generally accounted for at cost until they are settled unless there is a decline in the fair value of the contract that is determined to be other than temporary.

As of December 31, 2002, the utility derivative commodity asset balance was \$60.3 million, the derivative commodity liability balance was \$50.1 million and the offsetting net regulatory liability was \$10.2 million. As of December 31, 2001, the utility derivative commodity asset balance was \$1.9 million, the derivative commodity liability balance was \$159.4 million and the offsetting net regulatory asset was \$157.5 million. Utility derivative assets and liabilities, as well as the offsetting net regulatory asset or liability, can change significantly from period to period due to the settlement of contracts, the entering of new contracts and changes in commodity prices. The derivative commodity asset balance is included in Deferred Charges – Utility energy commodity derivative assets and the derivative commodity liability balance is included in Non-Current Liabilities and Deferred Credits – Utility energy commodity derivative liabilities on the Consolidated Balance Sheet. The offsetting net regulatory asset is included in Deferred Charges – Other regulatory assets and the offsetting net regulatory liability is included in Non-Current Liabilities and Deferred Credits – Other non-current liabilities and deferred credits on the Consolidated Balance Sheet.

Interpretations that may be issued by the Derivatives Implementation Group, a task force created to assist the FASB in answering questions that companies have in implementing SFAS No. 133, may change the conclusions that the Company has reached regarding accounting for energy contracts. As a result, the accounting treatment and financial statement impact could change in future periods.

NOTE 8. ENERGY COMMODITY TRADING

The Company's energy-related businesses are exposed to risks relating to, but not limited to, changes in certain commodity prices and counterparty performance. In order to manage the various risks relating to these exposures, Avista Utilities utilizes electric, natural gas and related derivative commodity instruments, such as forwards, futures, swaps and options, and Avista Energy engages in the trading of such instruments. Avista Utilities and Avista Energy have policies and procedures to manage risks inherent in these activities. The Company has a Risk Management Committee, separate from the units that create such risk exposure, that is overseen by the Audit Committee of the Company's Board of Directors, to monitor compliance with the Company's risk management policies and procedures.

Avista Utilities

Avista Utilities sells and purchases electric capacity and energy at wholesale to and from utilities and other entities under long-term contracts having terms of more than one year. In addition, Avista Utilities engages in an ongoing process of resource optimization which involves short-term purchases and sales in the wholesale market in pursuit of an economic selection of resources to serve retail and wholesale loads. Avista Utilities makes continuing projections of (1) future retail and wholesale loads based on, among other things, forward estimates of factors such as customer usage and weather as well as historical data and contract terms and (2) resource availability based on, among other things, estimates of streamflows, generating unit availability, historic and forward market information and experience. On the basis of these continuing projections, Avista Utilities purchases and sells energy on an annual, quarterly, monthly, daily and hourly basis to match actual resources to actual energy requirements. This process includes hedging transactions.

Avista Utilities manages the impact of fluctuations in electric energy prices by establishing volume limits for the imbalance between projected loads and resources and through the use of derivative commodity instruments for hedging purposes. Any imbalance is required to remain within limits, or management action or decisions are triggered to address larger imbalance situations and manage the exposure to market risk. Avista Energy is responsible for the daily management of natural gas supplies to meet the requirements of Avista Utilities' customers in the states of Washington, Idaho and Oregon.

In addition, Avista Utilities utilizes derivative commodity instruments for hedging price risk associated with natural gas. The Risk Management Committee has limited the types of commodity instruments Avista Utilities may use to those related to electricity and natural gas commodities and those instruments are to be used for hedging price fluctuations associated with the management of energy resources owned or controlled by Avista Utilities. The market values of natural gas derivative commodity instruments held by Avista Utilities as of December 31, 2002 and 2001, were a \$24.6 million net liability and a \$133.2 million net liability, respectively. The significant liability position as of December 31, 2001 was a result of forward commitments to purchase natural gas entered into during 2000 and the first part of 2001 at prices in excess of the market price for natural gas as of December 31, 2001. The decrease from December 31, 2001 to December 31, 2002 reflects the settlement of contracts during the period as well as an increase in the forward price of natural gas. Realized losses are reflected as adjustments through purchased gas cost adjustments, the ERM or the PCA mechanism.

Avista Energy

Avista Energy accounted for energy commodity trading activity in compliance with EITF Issue No. 98-10 through December 31, 2002 for contracts entered into on or prior to October 25, 2002. In October 2002, the EITF rescinded Issue No. 98-10. As such, Avista Energy is required to account for energy trading contracts that meet the definition of a derivative in compliance with SFAS No. 133 effective January 1, 2003 for all contracts entered into prior to October 25, 2002, and effective immediately for all contracts entered into subsequent to October 25, 2002. Contracts not meeting the definition of a derivative are accounted for on an accrual basis. See Note 2 for further details.

Avista Energy purchases natural gas and electricity from producers and other trading companies, and its customers include commercial and industrial end-users, electric utilities, natural gas distribution companies, and other trading companies. Avista Energy's marketing and energy risk management services are provided through the use of a variety of derivative commodity contracts to purchase or supply natural gas and electric energy at specified delivery points and at specified future dates. Avista Energy trades natural gas and electricity derivative commodity instruments on national exchanges and through other unregulated exchanges and brokers from whom these commodity derivatives are available, and therefore experiences net open positions in terms of price, volume, and specified delivery point. The open positions expose Avista Energy to the risk that fluctuating market prices may adversely impact its financial condition or results of operations. However, the net open position is actively managed with strict policies designed to limit the exposure to market risk and requires daily reporting to management of potential financial exposure.

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

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

Avista Energy's trading activities are subject to mark-to-market accounting, under which changes in the market value of outstanding electric, natural gas and related derivative commodity instruments are recognized as unrealized gains or losses in the period of change. Market prices are utilized in determining the value of the electric, natural gas and related derivative commodity instruments. For natural gas commodity instruments, these market prices are generally available through three years. For electric commodity instruments, these market prices are generally available through two years. For longer-term positions and certain short-term positions for which market prices are not available, a model to estimate forward price curves is utilized. Gains and losses on electric, natural gas and related derivative commodity instruments utilized for trading are recognized in income on a current basis (the mark-to-market method) and are included in the Consolidated Statements of Income and Comprehensive Income in operating revenues on a net basis, and in the Consolidated Balance Sheets as current or non-current energy commodity assets or liabilities. Contracts in a receivable position, as well as the options held, are reported as assets. Similarly, contracts in a payable position, as well as options written, are reported as liabilities. Net cash flows are recognized in the period of settlement.

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

The contract or notional amounts and terms of Avista Energy's derivative commodity investments outstanding as of December 31, 2002 are set forth below (in thousands of mmBTUs and MWhs):

	Fixed Price Payor	Fixed Price Receiver	Maximum Terms in Years	Index Price Payor	Index Price Receiver	Maximum Terms in Years
Energy commodities (volumes)						
Natural gas	91,194	86,400	7	620,490	610,946	2
Electric	92,063	91,091	14	259	19	2

Contract or notional amounts reflect the volume of transactions, but do not necessarily represent the dollar amounts exchanged by the parties to the derivative commodity instruments. Accordingly, contract or notional amounts do not accurately measure Avista Energy's exposure to market or credit risks. The maximum terms in years detailed above are not indicative of likely future cash flows as these positions may be offset in the markets at any time.

Estimated Fair Value The estimated fair value of Avista Energy's derivative commodity instruments outstanding as of December 31, 2002, and the average estimated fair value of those instruments held during the year ended December 31, 2002, are set forth below (dollars in thousands):

	Estimated Fair Value as of December 31, 2002				Average Estimated Fair Value for the year ended December 31, 2002			
	Current Assets	Long-term Assets	Current Liabilities	Long-term Liabilities	Current Assets	Long-term Assets	Current Liabilities	Long-term Liabilities
Natural gas	$143,730	$ 38,198	$111,763	$ 35,445	$144,090	$ 50,945	$117,236	$ 38,103
Electric	221,747	310,111	193,018	278,759	223,534	287,010	167,197	247,476
Total	$365,477	$348,309	$304,781	$314,204	$367,624	$337,955	$284,433	$285,579

The weighted average term of Avista Energy's natural gas derivative commodity instruments as of December 31, 2002 was approximately 4 months. The weighted average term of Avista Energy's electric derivative commodity instruments as of December 31, 2002 was approximately 7 months. The change in the estimated fair value position of Avista Energy's energy commodity portfolio, net of the reserves for credit and market risk for 2002 was an unrealized loss of $91.9 million and is included in the Consolidated Statements of Income and Comprehensive Income in operating revenues. The change in the fair value position for 2001 was an unrealized loss of $30.2 million. In 2000, an unrealized gain of $176.8 million was recorded.

Avista Energy reports the net margin on trading activities in operating revenues in the Consolidated Statements of Income and Comprehensive Income. The following table presents the gross amount of realized sales contracts for Avista Energy in both the dollar amount and volume of transactions for the years ended December 31:

	2002	2001	2000
Gross Realized Sales Transactions (dollars in thousands):			
Electric	$1,417,499	$3,380,058	$4,721,291
Natural gas	958,183	1,619,285	1,751,264
Other	-	1,612	58,996
Total gross settled transactions	$2,375,682	$5,000,955	$6,531,551
Gross Realized Sales Volume:			
Electric (thousands of MWhs)	40,426	47,927	105,548
Natural gas (thousands of dekatherms)	225,983	248,193	273,448

Market Risk

Market risk is, in general, the risk of fluctuation in the market price of the commodity being traded and is influenced primarily by supply and demand. Market risk includes the fluctuation in the market price of associated derivative commodity instruments. Market risk is influenced to the extent that the performance or nonperformance by market participants of their contractual obligations and commitments affect the supply of, or demand for, the commodity.

Avista Utilities and Avista Energy manage, on a portfolio basis, the market risks inherent in their activities subject to parameters established by the Company's Risk Management Committee. Market risks are monitored by the Risk Management Committee to ensure compliance with the Company's risk management policies. Avista Utilities measures exposure to market risk through daily evaluation of the imbalance between projected loads and resources. Avista Energy measures the risk in its portfolio on a daily basis utilizing a VAR model and monitors its risk in comparison to established thresholds.

Credit Risk

Credit risk relates to the risk of loss that Avista Utilities and/or Avista Energy would incur as a result of non-performance by counterparties of their contractual obligations to deliver energy and make financial settlements. Credit risk includes not only the risk that a counterparty may default due to circumstances relating directly to it, but also the risk that a counterparty may default due to circumstances that relate to other market participants that have a direct or indirect relationship with such counterparty. Avista Utilities and Avista Energy seek to mitigate credit risk by applying specific eligibility criteria to existing and prospective counterparties and by actively monitoring current credit exposures. These policies include an evaluation of the financial condition and credit ratings of counterparties, collateral requirements or other credit enhancements, such as letters of credit or parent company guarantees, and the use of standardized agreements that allow for the netting or offsetting of positive and negative exposures associated with a single counterparty.

Avista Energy has concentrations of suppliers and customers in the electric and natural gas industries including electric utilities, natural gas distribution companies, and other energy marketing and trading companies. In addition, Avista Energy has concentrations of credit risk related to geographic location as Avista Energy operates in the western United States and western Canada. These concentrations of counterparties and concentrations of geographic location may impact Avista Energy's overall exposure to credit risk, either positively or negatively, in that the counterparties may be similarly affected by changes in economic, regulatory or other conditions.

Credit risk also involves the exposure that counterparties perceive related to performance by Avista Utilities and Avista Energy to perform deliveries and settlement of energy transactions. These counterparties may seek assurance of performance in the form of letters of credit, prepayment or cash deposits, and, in the case of Avista Energy, parent company (Avista Capital) performance guarantees. In periods of price volatility, the level of exposure can change significantly, with the result that sudden and significant demands may be made against the Company's capital resource reserves (credit facilities and cash). Avista Utilities and Avista Energy actively monitor the exposure to possible collateral calls and take steps to minimize capital requirements.

Other Operating Risks

In addition to commodity price risk, Avista Utilities' commodity positions are subject to operational and event risks including, among others, increases in load demand, transmission or transport disruptions, fuel quality specifications, forced outages at generating plants and disruptions to information systems and other administrative tools required for normal operations. Avista Utilities also has exposure to weather conditions and natural disasters that can cause physical damage to property, requiring immediate repairs to restore utility service.

NOTE 9. CASH DEPOSITS WITH AND FROM COUNTERPARTIES

Cash deposits from counterparties totaled $92.7 million and $15.7 million as of December 31, 2002 and 2001, respectively, and are included in other current liabilities on the Consolidated Balance Sheets. These funds are held by Avista Utilities and Avista Energy to mitigate the potential impact of counterparty default risk. These amounts are subject to return if conditions warrant because of continuing portfolio value fluctuations with those parties or substitution of collateral.

Cash deposited with counterparties totaled $35.7 million and $1.5 million as of December 31, 2002 and 2001, respectively, and are included in prepayments and other current assets on the Consolidated Balance Sheets.

As is common industry practice, Avista Utilities and Avista Energy maintain margin agreements with certain counterparties. Margin calls are triggered when exposures exceed predetermined contractual limits. Price movements in electricity and natural gas can generate exposure levels in excess of these contractual limits. From time to time, margin calls are made and/or received by Avista Utilities and Avista Energy. Negotiating for collateral in the form of cash, letters of credit, or parent company performance guarantees is a common industry practice.

NOTE 10. JOINTLY OWNED ELECTRIC FACILITIES

The Company has a 50 percent ownership interest in a combined cycle natural gas-fired turbine power plant, the Coyote Springs 2 Generation Plant (Coyote Springs 2) located in northcentral Oregon. It is expected that Coyote Springs 2 will commence operations in 2003. The Company's investment in Coyote Springs 2 was $109.0 million as of December 31, 2002. The Company's investment in Coyote Springs 2 was held by Avista Power as of December 31, 2002 and is included in Non-utility properties and investments in the Consolidated Balance Sheet. In January 2003, the Company's ownership interest in the plant was transferred from Avista Power to Avista Corp. to be operated as an asset of Avista Utilities. The Company's share of related fuel costs as well as operating and maintenance expenses for plant in service will be included in the corresponding accounts in the Consolidated Statements of Income and Comprehensive Income when Coyote Springs 2 commences operations.

The Company has a 15 percent ownership interest in a twin-unit coal-fired generating facility, the Colstrip Generating Project (Colstrip) located in southeastern Montana, and provides financing for its ownership interest in the project. The Company's share of related fuel costs as well as operating and maintenance expenses for plant in service is included in the corresponding accounts in the Consolidated Statements of Income and Comprehensive Income. The Company's share of utility plant in service for Colstrip was $316.0 million and accumulated depreciation was $158.6 million as of December 31, 2002.

NOTE 11. PROPERTY, PLANT AND EQUIPMENT

The balances of the major classifications of property, plant and equipment are detailed in the following table as of December 31 (dollars in thousands):

	2002	2001
Avista Utilities:		
Electric production	$ 740,736	$ 691,299
Electric transmission	295,284	288,739
Electric distribution	698,757	678,448
Construction work-in-progress (CWIP) and other	85,631	119,389
Electric total	1,820,408	1,777,875
Natural gas underground storage	18,285	18,130
Natural gas distribution	430,273	414,422
CWIP and other	44,675	46,404
Natural gas total	493,233	478,956
Common plant (including CWIP)	74,751	75,912
Total Avista Utilities	2,388,392	2,332,743
Energy Trading and Marketing	142,428	128,577
Information and Technology	15,294	16,030
Other	20,611	21,117
Total	$2,566,725	$2,498,467

Equipment under capital leases at Avista Utilities totaled $0.7 million as of December 31, 2002. The associated accumulated depreciation totaled $0.1 million as of December 31, 2002. Avista Utilities did not have any property, plant and equipment under capital leases as of December 31, 2001.

Property, plant, and equipment under capital leases at Avista Capital's subsidiaries totaled $3.3 million and $5.4 million as of December 31, 2002 and 2001, respectively. The associated accumulated depreciation totaled $2.1 million and $2.6 million as of December 31, 2002 and 2001, respectively.

NOTE 12. PENSION PLANS AND OTHER POSTRETIREMENT BENEFIT PLANS

The Company has a defined benefit pension plan covering substantially all of its regular full-time employees. Certain of the Company's subsidiaries also participate in this plan. Individual benefits under this plan are based upon years of service and the employee's average compensation as specified in the plan. The Company's funding policy is to contribute amounts that are not less than the minimum amounts required to be funded under the Employee Retirement Income Security Act, nor more than the maximum amounts which are currently deductible for income tax purposes. Pension fund assets are invested primarily in marketable debt and equity securities. As of December 31, 2002, the Company's pension plan had assets with a fair value that was less than the present value of the accumulated benefit obligation under the plan. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $33.4 million and an intangible asset of $6.4 million (representing the amount of unrecognized prior service cost) related to the pension plan. This resulted in a charge to other comprehensive income of $17.6 million, net of taxes of $9.4 million. The pension plan was amended effective July 1, 2002 to provide a lump sum payment option for collectively bargained employees.

The Company also has a Supplemental Executive Retirement Plan (SERP) that provides additional pension benefits to executive officers of the Company. The SERP is intended to provide benefits to executive officers whose benefits under the pension plan are reduced due to the application of Section 415 of the Internal Revenue Code of 1986 and the deferral of salary under deferred compensation plans. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $0.7 million related to the SERP. In 2001, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $1.1 million related to the SERP. This resulted in a charge to other comprehensive income of $0.5 million and $0.7 million, net of taxes, for 2002 and 2001, respectively.

The Company provides certain health care and life insurance benefits for substantially all of its retired employees. The Company accrues the estimated cost of postretirement benefit obligations during the years that employees provide services. The Company elected to amortize the transition obligation of $34.5 million over a period of twenty years, beginning in 1993.

The following table sets forth the pension and postretirement plan disclosures as of December 31, 2002 and 2001 and for the years ended December 31, 2002, 2001 and 2000 (dollars in thousands):

	Pension Benefits		Post-retirement Benefits	
	2002	2001	2002	2001
Change in benefit obligation:				
Benefit obligation as of beginning of year	$210,510	$184,636	$36,355	$32,761
Service cost	6,734	5,716	304	460
Interest cost	15,119	14,293	2,184	2,567
Plan amendment	(2,530)	-	(5,821)	-
Actuarial loss (gain)	22,243	18,582	(660)	3,267
Benefits paid	(12,229)	(11,780)	(3,091)	(2,635)
Expenses paid	(1,462)	(937)	(209)	(65)
Benefit obligation as of end of year	$238,385	$210,510	$29,062	$36,355
Change in plan assets:				
Fair value of plan assets as of beginning of year	$153,705	$175,033	$13,969	$15,196
Actual return on plan assets	(16,677)	(9,313)	(1,451)	(902)
Employer contributions	12,000	-	-	511
Benefits paid	(11,441)	(11,078)	(1,008)	(771)
Expenses paid	(1,462)	(937)	(209)	(65)
Fair value of plan assets as of end of year	$136,125	$153,705	$11,301	$13,969
Funded status	$(102,260)	$(56,805)	$(17,761)	$(22,386)
Unrecognized net actuarial loss (gain)	79,812	31,144	1,425	(429)
Unrecognized prior service cost	6,366	9,726	-	-
Unrecognized net transition obligation/(asset)	(2,671)	(3,757)	9,788	16,865
Accrued benefit cost	(18,753)	(19,692)	(6,548)	(5,950)
Additional minimum liability	(35,303)	(1,139)	-	-
Accrued benefit liability	$(54,056)	$(20,831)	$(6,548)	$(5,950)

	Pension Benefits		Post-retirement Benefits	
	2002	2001	2002	2001
Assumptions as of December 31				
Discount rate	6.75%	7.25%	6.75%	7.25%
Expected long-term return on plan assets	8.00%	9.00%	8.00%	9.00%
Rate of compensation increase	5.00%	5.00%		
Medical cost trend pre-age 65 – initial			9.00%	9.00%
Medical cost trend pre-age 65 – ultimate			5.00%	5.00%
Ultimate medical cost trend year pre-age 65			2007	2003
Medical cost trend post-age 65 – initial			10.00%	12.00%
Medical cost trend post-age 65 – ultimate			6.00%	6.00%
Ultimate medical cost trend year post-age 65			2007	2004

	2002	2001	2000	2002	2001	2000
Components of net periodic benefit cost:						
Service cost	$ 6,734	$ 5,716	$ 5,372	$ 304	$ 460	$ 601
Interest cost	15,119	14,293	13,412	2,184	2,567	2,407
Expected return on plan assets	(12,311)	(15,254)	(16,243)	(1,064)	(1,311)	(1,372)
Transition (asset)/obligation recognition	(1,086)	(1,086)	(1,086)	1,256	1,534	1,534
Amortization of prior service cost	831	989	1,548	-	-	-
Net gain recognition	1,021	139	(858)	-	(52)	(300)
Net periodic benefit cost	$10,308	$ 4,797	$ 2,145	$2,680	$3,198	$2,870

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point increase in the assumed health care cost trend rate for each year would increase the accumulated postretirement benefit obligation as of December 31, 2002 by $2.0 million and the service and interest cost by $0.2 million. A one-percentage-point decrease in the assumed health care cost trend rate for each year would decrease the accumulated postretirement benefit obligation as of December 31, 2002 by $1.7 million and the service and interest cost by $0.2 million.

The Company has a salary deferral 401(k) plan that is a defined contribution plan and covers substantially all employees. Employees can make contributions to their respective accounts in the 401(k) plan on a pre-tax basis up to the maximum amount permitted by law. The Company matches a portion of the salary deferred by each participant according to the schedule in the 401(k) plan. Employer matching contributions of $3.4 million, $3.5 million, $3.3 million were expensed in 2002, 2001 and 2000, respectively.

NOTE 13. ACCOUNTING FOR INCOME TAXES

As of December 31, 2002 and 2001, the Company had net regulatory assets of $139.1 million and $149.0 million, respectively, related to the probable recovery of certain deferred tax liabilities from customers through future rates.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes and tax credit carryforwards. The net deferred income tax liability consisted of the following as of December 31 (dollars in thousands):

	2002	2001
Deferred tax assets:		
Allowance for doubtful accounts	$ 16,343	$ 17,431
Reserves not currently deductible	15,750	11,071
Contributions in aid of construction	9,709	9,176
Deferred compensation	4,112	4,481
Centralia sale regulatory liability	2,954	3,415
Unfunded accumulated benefit obligation	9,736	399
Other	7,172	9,544
Total deferred tax assets	65,776	55,517

	2002	2001
Deferred tax liabilities:		
Differences between book and tax basis of utility plant	364,827	367,406
Power and natural gas deferrals	58,081	88,323
Unrealized energy commodity gains	34,231	66,401
Power exchange contract	44,533	34,444
Demand side management programs	5,064	5,679
Loss on reacquired debt	8,781	4,696
Other	4,406	5,996
Total deferred tax liabilities	519,923	572,945
Net deferred tax liability	$454,147	$517,428

The realization of deferred tax assets is dependent upon the ability to generate taxable income in future periods. The Company evaluated available evidence supporting the realization of its deferred tax assets and determined it is more likely than not that deferred tax assets will be realized.

A reconciliation of federal income taxes derived from statutory federal tax rates (35 percent in 2002, 2001 and 2000) applied to pre-tax income from continuing operations as set forth in the accompanying Consolidated Statements of Income and Comprehensive Income is as follows for the years ended December 31 (dollars in thousands):

	2002	2001	2000
Federal income taxes at statutory rates	$22,506	$32,897	$62,319
Increase (decrease) in tax resulting from:			
Accelerated tax depreciation	5,166	5,849	4,835
State income tax expense	2,348	(8,870)	3,712
Prior year audit adjustments	-	(395)	72
Other-net	(26)	4,905	6,060
Total income tax expense	$29,994	$34,386	$76,998
Income Tax Expense Consisted of the Following:			
Federal taxes currently provided	$70,281	$(44,755)	$(4,839)
Deferred federal income taxes	(40,287)	79,141	81,837
Total income tax expense	$29,994	$34,386	$76,998
Income Tax Expense by Business Segment:			
Avista Utilities	$32,137	$20,177	$(1,990)
Energy Trading and Marketing	12,311	32,489	95,266
Information and Technology	(7,144)	(11,977)	(10,138)
Other	(7,310)	(6,303)	(6,140)
Total income tax expense	$29,994	$34,386	$76,998

NOTE 14. ENERGY PURCHASE CONTRACTS

The Company has contracts related to the purchase of fuel for thermal generation, natural gas and hydroelectric power. The termination dates of the contracts range from one month to the year 2044. The Company also has various agreements for the purchase, sale or exchange of electric energy with other utilities, cogenerators, small power producers and government agencies. Total expenses for power purchased, natural gas purchased, fuel for generation and other fuel costs were $382.4 million, $1,054.2 million and $1,312.7 million in 2002, 2001 and 2000, respectively. The following table details future contractual commitments for power resources (including transmission contracts) and natural gas resources (including transportation contracts) (dollars in thousands):

	2003	2004	2005	2006	2007	Thereafter	Total
Power resources	$194,873	$118,775	$ 65,349	$ 64,580	$ 66,476	$506,472	$1,016,525
Natural gas resources	195,580	171,470	82,393	48,175	48,172	385,375	931,165
Total	$390,453	$290,245	$147,742	$112,755	$114,648	$891,847	$1,947,690

All of the energy purchase contracts were entered into as part of Avista Utilities' obligation to serve its retail natural gas and electric customers' energy requirements. As a result, these costs are generally recovered either through base retail rates or adjustments to retail rates as part of the power and natural gas cost deferral and recovery mechanisms.

In addition, the Company has operational agreements, settlements and other contractual obligations with respect to its generation, transmission and distribution facilities. The expenses associated with these agreements are reflected as operation and maintenance expenses in the Consolidated Statements of Income and Comprehensive Income. The following table details future contractual commitments with respect to these agreements (dollars in thousands):

	2003	2004	2005	2006	2007	Thereafter	Total
Contractual obligations	$10,345	$12,406	$12,405	$12,406	$12,405	$185,353	$245,320

The Company has fixed contracts with certain Public Utility Districts (PUD) to purchase portions of the output of certain generating facilities. Although the Company has no investment in the PUD generating facilities, the fixed contracts obligate the Company to pay certain minimum amounts (based in part on the debt service requirements of the PUD) whether or not the facility is operating. The cost of power obtained under the contracts, including payments made when a facility is not operating, is included in resource costs in the Consolidated Statements of Income and Comprehensive Income. Expenses under these PUD contracts for 2002, 2001 and 2000, were $7.8 million, $7.4 million and $7.5 million, respectively.

Information as of December 31, 2002, pertaining to these PUD contracts is summarized in the following table (dollars in thousands):

	Company's Current Share of					
	Output	Kilowatt Capability	Annual Costs (1)	Debt Service Costs (1)	Bonds Outstanding	Expiration Date
Chelan County PUD:						
Rocky Reach Project	2.9%	37,000	$1,842	$623	$4,053	2011
Douglas County PUD:						
Wells Project	3.5	30,000	1,100	587	5,465	2018
Grant County PUD:						
Priest Rapids Project	6.1	55,000	1,768	910	9,662	2040
Wanapum Project	8.2	75,000	3,096	1,754	12,153	2040
Totals		197,000	$7,806	$3,874	$31,333	

(1) The annual costs will change in proportion to the percentage of output allocated to the Company in a particular year. Amounts represent the operating costs for the year 2002. Debt service costs are included in annual costs.

The estimated aggregate amounts of required minimum payments (the Company's share of existing debt service costs) under these PUD contracts are as follows (dollars in thousands):

	2003	2004	2005	2006	2007	Thereafter	Total
Minimum payments	$4,277	$3,249	$3,402	$2,759	$2,887	$22,041	$38,615

In addition, the Company will be required to pay its proportionate share of the variable operating expenses of these projects.

Avista Energy has contractual commitments to purchase energy commodities in future periods. The following table details future contractual commitments for Avista Energy's physical and financial energy contracts (dollars in thousands):

	2003	2004	2005	2006	2007	Thereafter	Total
Physical contracts	$ 935,954	$323,700	$206,400	$188,174	$126,028	$393,106	$2,173,362
Financial contracts	960,700	89,008	2,505	11,842	-	-	1,064,055
Total	$1,896,654	$412,708	$208,905	$200,016	$126,028	$393,106	$3,237,417

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

NOTE 15. LONG-TERM DEBT

The following details the interest rate and maturity dates of Secured and Unsecured Medium-Term Notes outstanding as of December 31 (dollars in thousands):

	Secured Medium-Term Notes			Unsecured Medium-Term Notes		
Maturity Year	Interest Rate	2002	2001	Interest Rate	2002	2001
2002	-	$ -	$ *	-	$ -	$ *
2003	6.25%	15,000	15,000	6.75%-9.13%	56,250	190,000
2004	-	-	-	7.42%	30,000	30,000
2005	6.39%-6.68%	29,500	29,500	-	-	-
2006	7.89%-7.90%	30,000	30,000	8.14%	8,000	8,000
2007	-	-	-	5.99%-7.94%	26,000	26,000
2008	6.89%-6.95%	20,000	20,000	6.06%	25,000	25,000
2010	6.67%-6.90%	10,000	10,000	8.02%	25,000	25,000
2012	7.37%	7,000	7,000	8.05%	12,000	12,000
2018	7.26%-7.45%	27,500	27,500	-	-	-
2022	-	-	-	8.15%-8.23%	10,000	10,000
2023	7.18%-7.54%	24,500	24,500	7.99%	5,000	5,000
2028	-	-	-	6.37%-6.88%	35,000	45,000
Total		$163,500	$163,500		$232,250	$376,000

* In 2001, the Company legally defeased $50.0 million of Medium-Term Notes scheduled to mature in 2002.

During 2002, the Company repurchased $133.8 million of Medium-Term Notes scheduled to mature in 2003, $59.8 million of Unsecured Senior Notes scheduled to mature in 2008 and $10.0 million of Medium-Term Notes scheduled to mature in 2028. In accordance with regulatory accounting practices, total net premiums paid to repurchase debt were $9.5 million and are being amortized over the average remaining maturity of outstanding debt.

In addition to the required maturities documented in the table above, the Company has sinking fund requirements of $3.1 million in 2003, $3.0 million in each of 2004 and 2005, $2.7 million in 2006 and $2.4 million in 2007. Under its Mortgage and Deed of Trust, the Company's sinking fund requirements may be met by certification of property additions at the rate of 143 percent of requirements. All of the Company's utility plant is subject to the lien of the Mortgage and Deed of Trust securing outstanding First Mortgage Bonds.

In April 2001, the Company issued $400.0 million of 9.75 percent Senior Notes due in 2008. In December 2001, the Company issued $150.0 million of 7.75 percent First Mortgage Bonds due in 2007.

As of December 31, 2002, the Company had remaining authorization to issue up to $317.0 million of Unsecured Medium-Term Notes.

Under various financing agreements, the Company is restricted as to the amount of additional First Mortgage Bonds that it can issue. As of December 31, 2002, the Company could issue $109.4 million of additional First Mortgage Bonds under the most restrictive of these financing agreements.

In September 1999, $83.7 million of Pollution Control Revenue Refunding Bonds (Avista Corporation Colstrip Project), Series 1999A due 2032 and Series 1999B due 2034 were issued by the City of Forsyth, Montana. The proceeds of the bonds were utilized to refund the $66.7 million of 7.13 percent First Mortgage Bonds due 2013 and the $17.0 million of 7.40 percent First Mortgage Bonds due 2016. The Series 1999A and Series 1999B Bonds are backed by an insurance policy issued by AMBAC Assurance Corporation. In January 2002, the interest rate on the bonds was fixed for a period of seven years at a rate of 5.00 percent for Series 1999A and 5.13 percent for Series 1999B.

Other long-term debt consisted of the following items as of December 31 (dollars in thousands):

	2002	2001
Notes payable	$ -	$ 688
Capital lease obligations	1,618	2,101
Subsidiary total debt	1,618	2,789
Less: current portion	651	1,827
Other long-term debt	$ 967	$ 962

NOTE 16. SHORT-TERM BORROWINGS

As of December 31, 2002, the Company maintained a committed line of credit with various banks in the total amount of $225.0 million that expires on May 20, 2003. The Company may have up to $50.0 million in letters of credit outstanding under this committed line of credit. As of December 31, 2002 and 2001, there were $14.3 million and $13.9 million of letters of credit outstanding, respectively. The Company pays commitment fees of up to 0.2 percent per annum on the average daily unused portion of the credit agreement, and utilization fees of up to 0.5 percent.

The committed line of credit agreement contains customary covenants and default provisions, including covenants not to permit the ratio of "consolidated total debt" to "consolidated total capitalization" of Avista Corp. to be greater than 65 percent at the end of any fiscal quarter. As of December 31, 2002, the Company was in compliance with this covenant with a ratio of 54.3 percent. The committed line of credit also has a covenant requiring the ratio of "earnings before interest, taxes, depreciation and amortization" to "interest expense" of Avista Utilities for the year ending December 31, 2002 to be greater than 1.6 to 1. As of December 31, 2002, the Company was in compliance with this covenant with a ratio of 2.04 to 1.

The Company had a commercial paper program that also provided for fixed-term loans during 2000 and 2001. None of these agreements were in place as of December 31, 2002 and 2001.

Balances and interest rates of bank borrowings under these arrangements were as follows as of and for the years ended December 31 (dollars in thousands):

	2002	2001	2000
Balance outstanding at end of period:			
Fixed-term loans	$ -	$ -	$ -
Commercial paper	-	-	11,160
Revolving credit agreement	30,000	55,000	152,000
Maximum balance outstanding during the period:			
Fixed-term loans	$ -	$ -	$ 80,000
Commercial paper	-	11,160	36,900
Revolving credit agreement	90,000	223,000	185,000
Average balance outstanding during the period:			
Fixed-term loans	$ -	$ -	$ 19,538
Commercial paper	-	558	16,833
Revolving credit agreement	47,027	108,996	84,255
Average interest rate during the period:			
Fixed-term loans	-%	-%	6.70%
Commercial paper	-	7.80	6.82
Revolving credit agreement	3.59	5.95	7.26
Average interest rate at end of period:			
Fixed-term loans	-%	-%	-%
Commercial paper	-	-	7.63
Revolving credit agreement	3.39	5.42	7.55

As of December 31, 2002, Avista Energy and its subsidiary, Avista Energy Canada, Ltd., as co-borrowers, had a credit agreement with a group of banks in the aggregate amount of $110.0 million, expiring June 30, 2003. This credit agreement may be terminated by the banks at any time and all extensions of credit under the agreement are payable upon demand, in either case at the lenders' sole discretion. This agreement also provides, on an uncommitted basis, for the issuance of letters of credit to secure contractual obligations to counterparties. This facility is guaranteed by Avista Capital and secured by Avista Energy's assets. The maximum amount of credit extended by the banks for the issuance of letters of credit is the subscribed amount of the facility less the amount of outstanding cash advances, if any. The maximum amount of credit extended by the banks for cash advances is $30.0 million. No cash advances were outstanding as of December 31, 2002. Letters of credit in the aggregate amount of $17.4 million were outstanding as of December 31, 2002. Under a similar credit facility that expired in June 2002, there were no cash advances outstanding and $39.6 million in letters of credit were outstanding as of December 31, 2001.

The Avista Energy credit agreement contains customary covenants and default provisions, including covenants to maintain "minimum net working capital" and "minimum net worth", as well as a covenant limiting the amount of indebtedness which the co-borrowers may incur. Avista Energy was in compliance with the covenants of its credit agreement as of December 31, 2002. Covenants in Avista Energy's credit agreement also restrict the amount of cash dividends that can be distributed to Avista Capital and ultimately to Avista Corp. During 2002, Avista Energy paid $116.4 million in dividends to Avista Capital.

In October 2001, Avista Capital entered into a one-year $20 million promissory note collateralized by certain receivables. The note was extended in October 2002 and paid off during December 2002.

NOTE 17. INTEREST RATE SWAP AGREEMENTS

In order to lower interest payments during a period of declining interest rates, Avista Corp. entered into an interest rate swap agreement effective July 17, 2002 and terminating on June 1, 2008. This interest rate swap agreement effectively changes the interest rate on $25 million of Unsecured Senior Notes from a fixed rate of 9.75 percent to a variable rate based on LIBOR. This interest rate swap agreement is designated as a fair value hedge, which hedges the variability of the fair value of the long-term debt attributable to interest rate risk. This interest rate swap agreement meets the conditions of a highly effective fair value hedge in accordance with SFAS No. 133. As such, this hedge is accounted for by recording the fair value of the interest rate swap on the balance sheet as either an asset or liability with a corresponding offset recorded to mark the Unsecured Senior Notes to fair value. The fair value of the interest rate swap was a $1.4 million asset as of December 31, 2002, which is included in other deferred charges in the Consolidated Balance Sheet.

Rathdrum Power, LLC (RP LLC), an unconsolidated entity that is 49 percent owned by Avista Power, operates a 270 MW natural gas-fired combustion turbine plant in northern Idaho (Lancaster Project). As of December 31, 2002, RP LLC had $118.7 million of debt outstanding that is not included in the consolidated financial statements of the Company. There is no recourse to the Company with respect to this debt. RP LLC has entered into two interest rate swap agreements, maturing in 2006, to manage the risk that changes in interest rates may affect the amount of future interest payments. RP LLC agreed to pay fixed rates of interest with the differential paid or received under the interest rate swap agreements recognized as an adjustment to interest expense. These interest rate swap agreements are considered hedges against fluctuations in future cash flows associated with changes in interest rates in accordance with SFAS No. 133. The fair value of the interest rate swap agreements was determined by reference to market values obtained from various third party sources. Avista Power's 49 percent ownership interest in RP LLC is accounted for under the equity method of accounting. The effect on the financial statements for 2002 was a $1.3 million unrealized loss recorded as other comprehensive loss and a corresponding decrease in non-utility property and investments in the Consolidated Balance Sheet.

NOTE 18. LEASES

The Company has multiple lease arrangements involving various assets, with minimum terms ranging from one to twenty-five years and expiration dates from 2003 to 2020. The Company's most significant leased assets include the Rathdrum CT and the corporate office building. See Note 2 for a change in accounting with respect to the Rathdrum CT that will become effective July 1, 2003. Certain lease arrangements require the Company, upon the occurrence of specified events, to purchase the leased assets. The Company's management believes the likelihood of the occurrence of the specified events under which the Company could be required to purchase the leased assets is remote. Rental expense under operating leases for the years ended December 31, 2002, 2001 and 2000 was $21.7 million, $19.8 million and $16.2 million, respectively.

Future minimum lease payments required under operating leases having initial or remaining noncancelable lease terms in excess of one year as of December 31, 2002 were as follows (dollars in thousands):

Year ending December 31:	2003	2004	2005	2006	2007	Thereafter	Total
Minimum payments required	$15,132	$13,117	$8,834	$8,163	$7,314	$65,515	$118,075

The payments under the Avista Corp. capital leases are $0.2 million in each of 2003, 2004 and 2005, and $0.1 million in 2006.

The payments under the Avista Capital subsidiaries' capital leases are $0.7 million in 2003, $0.3 million in 2004 and $0.1 million in 2005.

NOTE 19. GUARANTEES

The $110.0 million credit agreement of Avista Energy and its subsidiary, Avista Energy Canada, Ltd., as co-borrowers, is guaranteed by Avista Capital and secured by Avista Energy's assets. This credit agreement expires on June 30, 2003; however, it may be terminated by the banks at any time and all extensions of credit under the agreement are payable upon demand, in either case at the lenders' sole discretion. This agreement also provides, on an uncommitted basis, for the issuance of letters of credit to secure contractual obligations to counterparties. No cash advances were outstanding as of December 31, 2002. Letters of credit in the aggregate amount of $17.4 million were outstanding as of December 31, 2002. Under a similar credit facility that was guaranteed by Avista Capital that expired in June 2002, there were no cash advances outstanding and $39.6 million in letters of credit were outstanding as of December 31, 2001.

In the course of the energy trading business, Avista Capital provides guarantees to other parties with whom Avista Energy may be doing business. The face value of all performance guarantees issued by Avista Capital for energy trading contracts at Avista Energy was $451.7 million and $1.2 billion as of December 31, 2002 and 2001, respectively. At any point in time, Avista Capital is only liable for the outstanding portion of the guarantee, which was $64.6 million and $91.6 million as of December 31, 2002 and 2001, respectively. Most guarantees do not have set expiration dates; however, either party may terminate the guarantee at any time with minimal written notice.

Avista Power, through its equity investment in RP LLC, is a 49 percent owner of the Lancaster Project, which commenced commercial operation in September 2001. Commencing with commercial operations, all of the output from the Lancaster Project is contracted to Avista Energy for 25 years through a Power Purchase Agreement. Avista Corp. has guaranteed the Power Purchase Agreement with respect to the performance of Avista Energy.

NOTE 20. PREFERRED STOCK-CUMULATIVE

On September 15, 2002, the Company made a mandatory redemption of 17,500 shares of preferred stock for $1.75 million. On September 15, 2003, 2004, 2005 and 2006, the Company must redeem 17,500 shares at $100 per share plus accumulated dividends through a mandatory sinking fund. As such, redemption requirements are $1.75 million in each of the years 2003 through 2006. The remaining shares must be redeemed on September 15, 2007. The Company has the right to redeem an additional 17,500 shares on each September 15 redemption date. Upon involuntary liquidation, all preferred stock will be entitled to $100 per share plus accrued dividends.

NOTE 21. CONVERTIBLE PREFERRED STOCK

In December 1998, as part of a dividend restructuring plan, the Company issued 1,540,460 shares of its $12.40 Convertible Preferred Stock, Series L (Series L Preferred Stock), in exchange for 15,404,595 shares of common stock, on the basis of a one-tenth interest in one share of preferred stock for each share of common stock. The Series L Preferred Stock had a liquidation preference of $182.8125 per share.

During 1999, the Company repurchased the equivalent of 32,250 shares of the Series L Preferred Stock. In February 2000, the Company exercised its option to convert all the remaining outstanding shares of Series L Preferred Stock into common stock. One share of Series L Preferred Stock equaled 10 depositary shares, also known as RECONS (Return-Enhanced Convertible Securities). The RECONS were also converted into common stock on the same conversion date. Each of the RECONS was converted into the following: 0.7205 shares of common stock, representing the optional conversion price; plus 0.0361 shares of common stock, representing the optional conversion premium; plus the right to receive $0.21 in cash, representing an amount equivalent to accumulated and unpaid dividends up until, but excluding, the conversion date. Cash payments were made in lieu of fractional shares.

NOTE 22. COMPANY-OBLIGATED MANDATORILY REDEEMABLE PREFERRED TRUST SECURITIES

In 1997, Avista Capital I, a business trust, issued $60.0 million of Preferred Trust Securities with an annual distribution rate of 7.875 percent. Concurrent with the issuance of the Preferred Trust Securities, Avista Capital I issued $1.9 million of Common Trust Securities to the Company. The sole assets of Avista Capital I are the Company's 7.875 percent Junior Subordinated Deferrable Interest Debentures, Series A, with a principal amount of $61.9 million. These debt securities may be redeemed at the Company's option on or after January 15, 2002 and mature January 15, 2037. The Company has not redeemed any of these Preferred Trust Securities as of December 31, 2002.

In 1997, Avista Capital II, a business trust, issued $50.0 million of Preferred Trust Securities with a floating distribution rate of LIBOR plus 0.875 percent, calculated and reset quarterly. The annual distribution rate paid during 2002 ranged from 2.30 percent to 2.96 percent. As of December 31, 2002, the annual distribution rate was 2.30 percent. Concurrent with the issuance of the Preferred Trust Securities, Avista Capital II issued $1.5 million of Common Trust Securities to the Company. The sole assets of Avista Capital II are the Company's Floating Rate Junior Subordinated Deferrable Interest Debentures, Series B, with a principal amount of $51.5 million. These debt securities may be redeemed at the Company's option on or after June 1, 2007 and mature June 1, 2037. In December 2000, the Company purchased $10.0 million of these Preferred Trust Securities.

The Company has guaranteed the payment of distributions on, and redemption price and liquidation amount in respect of, the Preferred Trust Securities to the extent that Avista Capital I and Avista Capital II have funds available for such payments from the respective debt securities. Upon maturity or prior redemption of such debt securities, the Trust Securities will be mandatorily redeemed. The Consolidated Statements of Capitalization reflect only $100.0 million of Preferred Trust Securities as of December 31, 2002 and 2001 as all intercompany transactions have been eliminated.

NOTE 23. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of the Company's long-term debt (including current-portion, but excluding notes payable and other) as of December 31, 2002 and 2001 was estimated to be $1,001.2 million, or 103 percent of the carrying value, and $1,160.2 million, or 99 percent of the carrying value, respectively. The fair value of the Company's mandatorily redeemable preferred stock as of December 31, 2002 and 2001 was estimated to be $29.3 million, or 88 percent of the carrying value, and $17.5 million, or 50 percent of the carrying value, respectively. The fair value of the Company's preferred trust securities as of December 31, 2002 and 2001 was estimated to be $89.6 million, or 90 percent of the carrying value, and $84.6 million, or 85 percent of the carrying value, respectively. These estimates were based on available market information.

NOTE 24. COMMON STOCK

In April 1990, the Company sold 1,000,000 shares of its common stock to the Trustee of the Investment and Employee Stock Ownership Plan for Employees of the Company (Plan) for the benefit of the participants and beneficiaries of the Plan. In payment for the shares of common stock, the Trustee issued a promissory note payable to the Company in the amount of $14.1 million. Dividends paid on the stock held by the Trustee, plus Company contributions to the Plan, if any, are used by the Trustee to make interest and principal payments on the promissory note. The balance of the promissory note receivable from the Trustee ($4.1 million as of December 31, 2002) is reflected as a reduction to common equity. The shares of common stock are allocated to the accounts of participants in the Plan as the note is repaid. During 2002, the cost recorded for the Plan was $6.0 million. Interest on the note payable to the Company, cash and stock contributions to the Plan and dividends on the shares held by the Trustee were $0.5 million, $1.6 million and $0.1 million, respectively during 2002.

In May 1999, the Company's Board of Directors authorized the Company to repurchase in the open market or through privately negotiated transactions up to an aggregate of 10 percent of its common stock and common stock equivalents over the next two years. The repurchased shares return to the status of authorized but unissued shares. During 1999 and 2000, the Company repurchased approximately 4.8 million common shares and 322,500 shares of Return-Enhanced Convertible Securities (equivalent to 32,250 shares of Convertible Preferred Stock, Series L). The combined repurchases of these two securities represented 9 percent of outstanding common stock and common stock equivalents. No common shares were repurchased during 2001 and 2002.

In November 1999, the Company adopted a shareholder rights plan pursuant to which holders of common stock outstanding on February 15, 1999, or issued thereafter, were granted one preferred share purchase right (Right) on each outstanding share of common stock. Each Right, initially evidenced by and traded with the shares of common stock, entitles the registered holder to purchase one one-hundredth of a share of preferred stock of the Company, without par value, at a purchase price of $70, subject to certain adjustments, regulatory approval and other specified conditions. The Rights will be exercisable only if a person or group acquires 10 percent or more of the outstanding shares of common stock or commences a tender or exchange offer, the consummation of which would result in the beneficial ownership by a person or group of 10 percent or more of the outstanding shares of common stock. Upon any such acquisition, each Right will entitle its holder to purchase, at the purchase price, that number of shares of common stock or preferred stock of the Company (or, in the case of a merger of the Company into another person or group, common stock of the acquiring person or group) that has a market value at that time equal to twice the purchase price. In no event will the Rights be exercisable by a person that has acquired 10 percent or more of the Company's common stock. The Rights may be redeemed, at a redemption price of $0.01 per Right, by the Board of Directors of the Company at any time until any person or group has acquired 10 percent or more of the common stock. The Rights expire on March 31, 2009. This plan replaced a similar shareholder rights plan that expired in February 2000.

The Company has a Dividend Reinvestment and Stock Purchase Plan under which the Company's shareholders may automatically reinvest their dividends and make optional cash payments for the purchase of the Company's common stock at current market value.

In March 2000, the Company began issuing shares of its common stock to the Employee Investment Plan rather than having the Plan purchase shares of common stock on the open market. In the fourth quarter of 2000, the Company also began issuing new shares of common stock for the Dividend Reinvestment and Stock Purchase Plan. During 2002, 2001 and 2000, a total of 408,799, 332,861 and 125,636 shares of common stock were issued, respectively, to these plans.

NOTE 25. EARNINGS PER COMMON SHARE

In February 2000, all outstanding shares of Series L Preferred Stock were converted into 11,410,047 shares of common stock. The weighted-average number of shares of common stock outstanding during 2000 related to the converted shares was 9,975,997. The cost of converting the Series L Preferred Stock into common stock totaled $21.3 million during the first quarter of 2000, with $18.1 million representing the optional conversion premium and $3.2 million attributable to the regular dividend on the preferred stock.

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

	2002	2001	2000
Numerator:			
Income from continuing operations	$34,310	$59,605	$101,055
Income (loss) from discontinued operations	1,145	(47,449)	(9,376)
Net income before cumulative effect of accounting change	35,455	12,156	91,679
Cumulative effect of accounting change	(4,148)	-	-
Net income	31,307	12,156	91,679
Deduct: Preferred stock dividend requirements	2,402	2,432	23,735
Income available for common stock	$28,905	$ 9,724	$ 67,944
Denominator:			
Weighted-average number of common shares outstanding-basic	47,823	47,417	45,690
Effect of dilutive securities:			
Restricted stock	2	5	101
Stock options	49	13	312
Weighted-average number of common shares outstanding-diluted	47,874	47,435	46,103

	2002	2001	2000
Earnings per common share, basic:			
Earnings per common share from continuing operations ...	$0.67	$1.21	$1.69
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.21	1.49
Loss per common share from cumulative effect of accounting change	(0.09)	-	-
Total earnings per common share, basic	$0.60	$0.21	$1.49
Earnings per common share, diluted:			
Earnings per common share from continuing operations ...	$0.67	$1.20	$1.67
Earnings (loss) per common share from discontinued operations	0.02	(1.00)	(0.20)
Earnings per common share before cumulative effect of accounting change	0.69	0.20	1.47
Loss per common share from cumulative effect of accounting change	(0.09)	-	-
Total earnings per common share, diluted	$0.60	$0.20	$1.47

NOTE 26. INFORMATION AND TECHNOLOGY SEGMENT INFORMATION

The Information and Technology line of business includes the results of Avista Advantage and Avista Labs. Additional financial information for each of these separate companies is provided as follows for the years ended December 31 (dollars in thousands):

	2002	2001	2000
Avista Advantage			
Operating Revenues	$16,911	$13,151	$4,971
Loss From Operations (pre-tax)	(6,363)	(15,098)	(14,482)
Net Loss	(4,253)	(10,748)	(11,022)
Avista Labs			
Operating Revenues	719	664	761
Loss From Operations (pre-tax)	(12,455)	(14,774)	(11,942)
Net Loss	(7,864)	(8,636)	(8,010)

NOTE 27. STOCK COMPENSATION PLANS

Avista Corp.

In 1998, the Company adopted and shareholders approved an incentive compensation plan, the Long-Term Incentive Plan (1998 Plan). Under the 1998 Plan, certain key employees, directors and officers of the Company and its subsidiaries may be granted stock options, stock appreciation rights, stock awards (including restricted stock) and other stock-based awards and dividend equivalent rights. The Company has available a maximum of 2.5 million shares of its common stock for grant under the 1998 Plan. The shares issued under the 1998 Plan are purchased by the trustee on the open market. Beginning in 2000, non-employee directors began receiving options under this plan.

In 2000, the Company adopted a Non-Officer Employee Long-Term Incentive Plan (2000 Plan), which was not required to be approved by shareholders. The provisions of the 2000 Plan are essentially the same as those under the 1998 Plan, except for the exclusion of directors and executive officers of the Company. The Company has available a maximum of 2.5 million shares of its common stock for grant under the 2000 Plan.

The Company accounts for stock based compensation using APB No. 25, "Accounting for Stock Issued to Employees," which requires the recognition of compensation expense on the excess, if any, of the market price of the stock at the date of grant over the exercise price of the option. As the exercise price for options granted under the 1998 Plan and the 2000 Plan was equal to the market price at the date of grant, there was no compensation expense recorded by the Company. SFAS No. 123, "Accounting for Stock-Based Compensation," requires the disclosure of pro forma net income and earnings per common share had the Company adopted the fair value method of accounting for stock options. Under this statement, the fair value of stock-based awards is calculated with option pricing models. These models require the use of subjective assumptions, including stock price volatility, dividend yield, risk-free interest rate and expected time to exercise. The fair value of options is estimated on the date of grant using the Black-Scholes option-pricing model.

As of December 31, 2002, there were 2.3 million shares available for future stock grants under the 1998 Plan and the 2000 Plan.

The following summarizes stock options activity under the 1998 Plan and the 2000 Plan for the years ended December 31:

	2002	2001	2000
Number of shares under stock options:			
Options outstanding at beginning of year	2,440,475	1,843,900	1,360,325
Options granted	569,800	781,900	623,200
Options exercised	-	(2,750)	(44,975)
Options canceled	(325,925)	(182,575)	(94,650)
Options outstanding at end of year	2,684,350	2,440,475	1,843,900
Options exercisable at end of year	1,192,775	883,075	581,025
Weighted average exercise price:			
Options granted	$10.51	$12.43	$23.03
Options exercised	-	$17.96	$18.53
Options canceled	$19.88	$19.22	$18.15
Options outstanding at end of year	$15.69	$17.49	$19.81
Options exercisable at end of year	$18.28	$19.28	$18.72
Weighted average fair value of options granted during the year	$ 3.43	$ 5.54	$12.02
Principal assumptions used in applying the Black-Scholes model:			
Risk-free interest rate	3.25%-4.96%	4.05%-5.13%	5.87%-6.87%
Expected life, in years	7	7	7
Expected volatility	47.13%	60.80%	58.47%
Expected dividend yield	4.61%	3.93%	2.34%

Information with respect to options outstanding and options exercisable as of December 31, 2002 was as follows:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (in years)	Number of Shares	Weighted Average Exercise Price
$10.17-$11.68	542,800	$10.25	9.8	-	$ -
$11.69-$14.61	694,600	11.80	8.9	173,650	11.80
$14.62-$17.53	587,600	17.16	6.7	405,275	17.26
$17.54-$20.45	329,875	18.75	5.5	316,775	18.70
$20.46-$23.37	494,275	22.56	7.5	267,475	22.58
$26.29-$29.22	35,200	27.19	5.5	29,600	26.95
Total	2,684,350	$15.69	7.9	1,192,775	$18.28

Avista Capital Companies

Certain subsidiaries of Avista Capital have employee stock incentive plans under which certain employees and directors of the Company and the subsidiaries are granted options to purchase subsidiary shares at prices no less than the fair market value on the date of grant. Options outstanding under these plans usually vest over periods of between three and five years from the date granted and terminate ten years from the date granted. Upon termination of employment, vested options may be exercised and the related subsidiary shares may be, but are not required to be, repurchased by the applicable subsidiary at estimated fair value.

Non-Employee Director Stock Plan

In 1996, the Company adopted and shareholders approved the Non-Employee Director Stock Plan (1996 Director Plan). Under the 1996 Director Plan, directors who are not employees of the Company receive two-thirds of their annual retainer in Avista Corp. common stock. The Company acquires the common stock in the open market. The Company has available a maximum of 150,000 shares of its common stock under the 1996 Director Plan and there were 85,937 shares available for future compensation to non-employee directors as of December 31, 2002.

NOTE 28. COMMITMENTS AND CONTINGENCIES

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

Federal Energy Regulatory Commission Inquiry

In February 2002, the FERC issued an order commencing a fact-finding investigation of potential manipulation of electric and natural gas prices in the California energy markets by multiple companies. On May 8, 2002, the FERC requested data and information with respect to certain trading strategies that companies may have engaged in. Specifically, the requests inquired as to whether or not the Company engaged in certain trading strategies that were the same or similar to those used by Enron Corporation (Enron) and its affiliates. These requests were made to all sellers of wholesale electricity and/or ancillary services in the Western Interconnection during 2000 and 2001, including Avista Corp. and Avista Energy. On May 22, 2002, Avista Corp. and Avista Energy filed their responses to this request indicating that they had engaged in sound business practices in accordance with established market rules, and that no information was evident from business records or employee interviews that would indicate that Avista Corp. or Avista Energy, or its employees, were knowingly engaged in these trading strategies, or any variant of the strategies.

On June 4, 2002, the FERC issued an additional order to Avista Corp. and three other companies requiring these companies to show cause within ten days as to why their authority to charge market-based rates should not be revoked. In this order, the FERC alleged that Avista Corp. failed to respond fully and accurately to the data request made on May 8, 2002. On June 14, 2002, Avista Corp. provided additional information in response to the June 4, 2002 FERC order to establish that its initial response was appropriate and adequate.

On August 13, 2002, the FERC issued an order to initiate an investigation into possible misconduct by Avista Corp. and Avista Energy and two affiliates of Enron: Enron Power Marketing, Inc. (EPMI) and Portland General Electric Corporation (PGE). The purpose of the investigation was to determine whether Avista Corp. and Avista Energy engaged in or facilitated certain Enron trading strategies, whether Avista Corp.'s or Avista Energy's role in transactions with EPMI and PGE resulted in the circumvention of a code of conduct governing transactions with affiliates, and the imposition of any appropriate remedies such as refunds and revocation of market-based rates. The investigation also explored whether the companies provided all relevant information in response to the May 8, 2002 data request.

In December 2002, the FERC staff, Avista Corp. and Avista Energy filed a joint motion announcing that the parties have reached an agreement in principle. In the joint motion, the FERC Trial Staff states that its investigation found no evidence that: (1) any executives or employees of Avista Utilities or Avista Energy knowingly engaged in or facilitated any improper trading strategy; (2) Avista Utilities or Avista Energy engaged in any efforts to manipulate the western energy markets during 2000 and 2001; (3) Avista Utilities or Avista Energy withheld relevant information from the Commission's inquiry into the western energy markets for 2000 and 2001.

In December 2002, the FERC's administrative law judge approved the joint motion, suspending the procedural schedule in the FERC investigation regarding Avista Corp. and Avista Energy. In January 2003, the FERC staff, Avista Corp. and Avista Energy filed a completed agreement in resolution of the proceeding with the administrative law judge. The parties requested that the administrative law judge certify the agreement and forward it to the FERC for acceptance following a 30-day comment period.

On February 19, 2003 the City of Tacoma (Tacoma) and California Parties (the Office of the Attorney General, the CPUC, and the California Electricity Oversight Board, filing jointly) filed comments in opposition to the agreement in resolution between the FERC staff, Avista Corp. and Avista Energy. PGE filed comments supporting the agreement in resolution, but took exception to how certain transactions were reported. On March 3, 2003, Avista Corp. and Avista Energy filed joint reply comments in response to the concerns raised by Tacoma, the California Parties, and PGE. The FERC Trial Staff filed separate reply comments supporting the agreement in resolution and responding to Tacoma, the California Parties and PGE. The reply comments of Avista Corp., Avista Energy and the FERC Staff also reiterated the request that the administrative law judge certify the agreement in resolution and forward it to the FERC for approval.

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

Beginning on June 17, 2002, the CFTC has issued several subpoenas directing Avista Corp. to produce certain materials, make employees available for questions and to respond to certain interrogatories. This relates to electricity and natural gas trades by Avista Corp. and any of its subsidiaries (including Avista Energy), involving "round trip trades," "wash trades," or "sell/buyback trades" and price reporting. The CFTC subpoena applies to both Avista Corp. and Avista Energy. The Company is cooperating with the CFTC and is providing the information requested by the CFTC.

Class Action Securities Litigation

On September 27, 2002, Ronald R. Wambolt filed a class action lawsuit in the United States District Court for the Eastern District of Washington against Avista Corp., Thomas M. Matthews, the former Chairman of the Board, President and Chief Executive Officer of the Company, Gary G. Ely, the current Chairman of the Board, President and Chief Executive Officer of the Company, and Jon E. Eliassen, the former Senior Vice President and Chief Financial Officer of the Company. On October 9, 2002, Gail West filed a similar class action lawsuit in the same court against the same parties. On November 7, 2002, Michael Atlas filed a similar class action lawsuit in the same court against the same parties. On November 21, 2002, Peter Arnone filed a similar class action lawsuit in the same court against the same parties. In their complaints, the plaintiffs assert violations of the federal securities laws in connection with alleged misstatements and omissions of material fact pursuant to Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. In particular, the plaintiffs allege that the Company failed to disclose certain business practices that Avista Corp. was allegedly engaging in with EPMI and PGE. For further information see "Federal Energy Regulatory Commission Inquiry" above. The plaintiffs assert that such alleged misstatements and omissions have occurred in the Company's filings with the Securities and Exchange Commission and other information made publicly available by the Company, including press releases. The class action lawsuits assert claims on behalf of all persons who purchased, converted, exchanged or otherwise acquired the Company's common stock during the period between November 23, 1999 and August 13, 2002. On February 3, 2003, the court issued an order consolidating the complaints under the name "In re Avista Corp. Securities Litigation," and on February 7, 2003 appointed the lead plaintiff and co-lead counsel. The Company intends to file a motion to dismiss these consolidated complaints and vigorously defend against these lawsuits.

California Energy Markets

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

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

In April 2002, the California AG provided notice of intent to file a complaint against Avista Energy in the California State Court on behalf of the State of California. As of the filing date of this report, the California AG has not filed the threatened complaint against Avista Energy. Complaints have been filed against approximately a dozen other companies, many of which have filed motions to dismiss based upon federal preemption and primary jurisdiction arguments. The threatened complaint alleges that Avista Energy failed to file rates and changes to rates charged for each sale of wholesale electricity in California markets with the FERC as required by Federal Power Act regulations and FERC orders. The threatened complaint asserts that each violation of law, regulation and order is an unlawful and unfair business practice under the California Business and Professions Code, subject to a penalty of $2,500 per violation. The threatened complaint further alleges that certain rates charged for wholesale electricity sold in California exceeded a just and reasonable rate. As such, the threatened complaint alleges that these rates violate the Federal Power Act and are also a violation under the California Business and Professions Code, subject to penalty. A significant portion of the transactions involved in this threatened complaint are also the subject of FERC proceedings to examine potential refunds and in most cases are transactions for which Avista Energy is still owed payment.

Washington Consumer Class Action Lawsuit

On December 23, 2002, Nick A. Symonds filed a class action lawsuit in the United States District Court for the Western District of Washington against numerous purchasers and sellers of wholesale electricity and natural gas in the western United States, including Avista Utilities. The class action lawsuit asserts claims on behalf of all persons and businesses residing in Washington who were purchasers of electric and/or natural gas energy from any period beginning in January 2000 to the present. The complaint alleges that due to the deregulation of the California energy market, the defendants were able to unlawfully manipulate the wholesale energy market resulting in supply shortages and high energy prices across the western United States, including Washington. The complaint further alleges that high energy prices have resulted in profits for the defendants at the expense of rate-paying consumers in Washington. The complaint seeks treble damages, attorney fees and costs, and an order that defendants immediately remedy the alleged unlawful practices relating to the purchase and sale of wholesale energy that affects rate-paying consumers in Washington. The complaint further seeks an order enjoining the defendants from continuing any alleged unlawful practices relating to the purchase and sale of wholesale energy that affects rate-paying consumers in Washington. The Company intends to file a motion to dismiss this complaint and vigorously defend against this lawsuit.

Enron Corporation

On December 2, 2001, Enron and certain of its affiliates filed for protection under chapter 11 of the United States Bankruptcy Code. Both Avista Corp. and Avista Energy had done considerable business and had short-term and long-term contracts with Enron affiliates. The bankruptcy filing constituted an event of default under contracts between Avista Corp. and Avista Energy, respectively, and certain Enron affiliates, namely, EPMI, Enron North America Company (ENA) and Enron Canada Corp. (ECC), that are guaranteed by Enron. As a result, Avista Corp. and Avista Energy terminated all of these contracts and suspended trading activities with all Enron affiliates, including the final position that was terminated and a settlement agreement reached between Avista Corp. and EPMI in October 2002.

As of December 31, 2002, Avista Energy had net accounts receivable of $13.9 million from EPMI and ENA. Avista Corp.'s and Avista Energy's contracts with each Enron affiliate provide that, upon termination, the net settlement of accounts receivable and accounts payable with such entity will be netted against the net mark-to-market value of the terminated forward contracts with such entity. It is estimated that for Avista Energy, netting the mark-to-market liability against the defaulted net accounts receivable will result in no significant loss due to non-collection from the Enron affiliates. The Company further estimates that the net mark-to-market liability to Enron affiliates with respect to the terminated forward contracts not yet settled (Avista Energy with EPMI and ENA) taken together, exceeds total net accounts receivable from these entities by less than $15 million.

In October 2002, Avista Corp. settled its remaining contract with EPMI with the approval of the U.S. Bankruptcy Court. In addition, Avista Corp. reached settlement agreements on all terminated positions with ECC and ENA. Avista Energy reached a settlement agreement on its terminated ECC positions. In each instance, the settlement agreements reached satisfy all of the Avista entity's obligations and exposure to such Enron entity. Confidentiality provisions contained in the settlement agreements protect disclosure of the specific details of each settlement. None of the settlements individually, nor all of the settlements collectively, have had or are expected to have a material adverse impact on Avista Corp.'s or Avista Energy's financial condition, results of operations or cash flows. All additional claims by the Enron entities for amounts that Avista Energy might owe with respect to the terminated forward contracts would be subject to any defenses and counterclaims which Avista Energy may have. Any residual obligation by Avista Energy for termination payments is not expected to have a material impact on the Company's financial condition, results of operations or cash flows. The Company continues to negotiate the settlement of other contracts with Enron affiliates.

The estimates of the mark-to-market values of terminated forward contracts are based on available broker quotes for the respective periods, and on assumptions as to future market prices and other information. While Avista Energy believes these assumptions are reasonable, they are subject to change and ultimately could be challenged by the Enron entities or their bankruptcy trustees, except as to those terminated forward contracts that have been fully settled by agreements among the parties as described above. The mark-to-market value of terminated contracts has not been firmly established and could result in undercollection that is not expected to be material to the financial condition, results of operations or cash flows of Avista Energy.

National Energy Production Corporation (NEPCO), a wholly owned subsidiary of Enron, was the contractor responsible for the engineering, procurement and construction of Coyote Springs 2. Avista Corp. owns 50 percent of Coyote Springs 2. NEPCO was not included in the initial bankruptcy filings made by Enron and its affiliates in December 2001. NEPCO subsequently filed for bankruptcy on May 20, 2002. However, Enron guaranteed NEPCO's obligations, and the bankruptcy filing by Enron was an event of default under the Coyote Springs 2 construction contract. As a result of this default and other defaults under the contract, NEPCO was removed as contractor for the project on April 15, 2002.

Avista Corp. is party to a power exchange arrangement which expires in 2016. Under this power exchange arrangement, EPMI purchases capacity from Avista Corp. and sells capacity to Spokane Energy LLC (Spokane Energy), a subsidiary of Avista Corp., formed in 1998 solely for the purpose of facilitating a long-term capacity contract between PGE and Avista Corp. The 1998 transaction resulted in the Company receiving $143.4 million in cash proceeds that was originally recorded as deferred revenue. Spokane Energy sells the related capacity to PGE. Subsequently, PGE became a subsidiary of Enron that has not been included in the bankruptcy filing to date. EPMI assisted in setting up the transaction structure and acts as an intermediary to abide by certain regulatory restrictions that currently prevent Spokane Energy and Avista Corp. from dealing directly with each other. The transaction is structured such that Spokane Energy bears full recourse risk for a loan (balance of $125.8 million as of December 31, 2002) that matures in January 2015 with no recourse to Avista Corp. related to the loan. EPMI is obligated to pay approximately $150,000 per month to Avista Corp. for its capacity purchase. EPMI defaulted on two payments to Avista Corp. prior to filing for bankruptcy. Such payments were accounted for and included in the settlement agreement reached between Avista Corp. and EPMI in October 2002.

Colorado River Commission of Nevada (CRCN) Complaint

On February 14, 2003, a complaint filed against Pioneer Companies, Inc. and numerous other defendants, including Avista Energy, was dismissed. The CRCN filed this complaint in the United States District Court for the District of Nevada in July 2002. CRCN is an agency of the State of Nevada, authorized to hold and administer rights to electric power generated on the Colorado River and from other sources. CRCN claimed it purchased power as a purported agent for Pioneer from numerous vendors, including Avista Energy. CRCN alleged that Pioneer had disavowed its contractual liability to pay for power due to be delivered for its benefit in the future, pursuant to transactions entered into for Pioneer's benefit by CRCN. CRCN alleged that it had funds available of approximately $35 million, resulting from the sale of options and energy originally secured by CRCN for the benefit of Pioneer, but believed the potential collective claims of all electricity vendors may have exceeded $100 million. Accordingly, CRCN was attempting to interplead into court the $35 million and asked the court to assess the competing claims of vendors to such funds. CRCN further requested that Pioneer be ordered to pay vendors amounts owed for transactions between CRCN (as Pioneer's agent) and vendors, and that such contracts are to be specifically enforced. Finally, CRCN was attempting to be indemnified against the future claims of vendors.

State of Washington Business and Occupation Tax

The State of Washington's Business and Occupation Tax applies to gross revenue from business activities. For most types of business, the tax applies to the gross sales price received for goods or services. For certain types of financial trading activities, including the sale of stocks, bonds and other securities, the tax applies to the realized gain from the sale of the financial asset. On an audit for the period from 1997 through June 2000, the Department of Revenue (DOR) took the position that approximately 20 percent of the forward energy trades of Avista Energy should not be treated as securities trades, but rather as energy deliveries. As a result, the DOR applied tax against the gross sales price of the energy contracts at issue. Avista Energy subsequently received an assessment of $14.5 million for tax and interest related to the disputed issue. It is the position of Avista Energy that all of its forward contract trading activities are substantively the same and there is no proper basis for the distinction made by the DOR. An administrative appeal was filed with the DOR and a hearing was held on September 25, 2001. The DOR issued a Proposed Determination on December 4, 2002, which reiterated the original $14.5 million assessment. At the present time Avista Energy is still in active negotiations with the DOR with respect to a Final Determination in this matter and believes that a satisfactory settlement can be reached. However, if a satisfactory settlement can not be reached, Avista Energy will have to record a charge and attempt to resolve the issue in court.

Sale of Pentzer Corporation Subsidiary

On February 26, 2001, IDX Corporation, formerly known as Store Fixtures Group, Inc., filed a complaint against Pentzer in the United States District Court for the District of Massachusetts, alleging breach of contract and negligent misrepresentation relating to a stock purchase agreement. Pursuant to this agreement, Pentzer sold the capital stock of a group of companies on August 31, 1999. Plaintiff alleges that Pentzer breached various representations and warranties concerning financial statements and inventory, contending that reliance on such representations and warranties caused them to pay more for the group of companies than they were worth. In total, plaintiff claims damages in the approximate amount of $7.8 million plus interest and attorney's fees. The Court approved the parties' joint motion to extend the discovery dates. The discovery process continues, as mediation that commenced during June 2002 has not been successful to date.

Montana Hydroelectric Security Act Initiative

In the November 5, 2002 General Election, Montana voters rejected an initiative that would have created a public agency to study whether it would benefit the people of Montana to have the state own and operate certain hydroelectric generating facilities located within the state. The initiative would have authorized the new public agency to acquire, through a negotiated purchase or an acquisition at fair market value through a condemnation proceeding, any or all hydroelectric facilities larger than 5 MW within the state. The Company's largest generation plant, the Noxon Rapids Hydroelectric Generating Station (Noxon Rapids) (527 MW), is located in Montana on the Clark Fork River.

Hamilton Street Bridge Site

A portion of the Hamilton Street Bridge Site in Spokane, Washington (including a former coal gasification plant site that operated for approximately 60 years until 1948) was acquired by the Company through a merger in 1958. The Company no longer owns the property. Initial core samples taken from the site indicated environmental contamination at the site. On January 15, 1999, the Company received notice from the State of Washington's Department of Ecology (DOE) that it had been designated as a potentially liable party (PLP) with respect to any hazardous substances located on this site, stemming from the Company's past ownership of the former gas plant site. In its notice, the DOE stated that it intended to complete an on-going remedial investigation of this site, complete a feasibility study to determine the most effective means of halting or controlling future releases of substances from the site, and to implement appropriate remedial measures. The Company responded to the DOE acknowledging its listing as a PLP, but requested that additional parties also be listed as PLPs. In the spring of 1999, the DOE named two other parties as additional PLPs.

An Agreed Order was signed by the DOE, the Company and another PLP, Burlington Northern & Santa Fe Railway Co. (BNSF) on March 13, 2000 that provided for the completion of a remedial investigation and a feasibility study. The work to be performed under the Agreed Order includes three major technical parts: completion of the remedial investigation; performance of a focused feasibility study; and implementation of an interim groundwater monitoring plan. During the second quarter of 2000, the Company received comments from the DOE on its initial remedial investigation, then submitted another draft of the remedial investigation, which was accepted as final by the DOE. After responding to comments from the DOE, the feasibility study was accepted by the DOE during the fourth quarter of 2000. After receiving input from the Company and the other PLPs, the final Cleanup Action Plan (CAP) was issued by the DOE on August 10, 2001. On September 10, 2001, the DOE issued an initial draft Consent Decree for the PLPs to review. During the first quarter of 2002, the Company and BNSF signed a cost sharing agreement. On September 11, 2002, the Company, BNSF and the DOE finalized the Consent Decree to implement the CAP. The third PLP has indicated it will not sign the Consent Decree. It is currently estimated that the Company's share of the costs will be less than $1.0 million. The Engineering and Design Report for the CAP was submitted to the DOE in January 2003. If approved by the DOE, it is anticipated that the CAP will be implemented in mid-2003. Negotiations are continuing with the third PLP with respect to the logistics of the CAP.

Spokane River

In March 2001, the DOE informed Avista Development, a subsidiary of Avista Capital, of a health advisory concerning PCBs found in fish caught in a portion of the Spokane River. In June 2001, Avista Development received official notice that it had been designated as a PLP with respect to contaminated sites on the Spokane River. The DOE discovered PCBs in fish and sediments in the Spokane River in the 1970s and 1980s. In the 1990s, the DOE performed subsequent sampling of the river and identified potential sources of the PCBs, including the Spokane Industrial Park (SIP) and a number of other entities in the area. The SIP, renamed Pentzer Development Corporation (Pentzer Development) in 1990, operated a wastewater treatment plant at the site until it was closed in December 1993. The SIP's treatment plant discharged to the Spokane River under the terms of a National Pollutant Discharge Elimination System permit issued by the DOE. Pentzer Development sold the property in 1996 and merged with Avista Development in 1998. Avista Development filed a response to this notice in August 2001. In December 2001, the DOE confirmed Avista Development's status as a PLP and named at least two other PLPs in this matter. During the first half of 2002, Avista and one other PLP met with the DOE to begin discussions and provide comments to the DOE on a draft Consent Decree and Scope of Work for a focused remedial investigation and feasibility study of the site. One other PLP has not been participating in negotiations. The Consent Decree and Scope of Work for the remedial investigation and feasibility study of the site were finalized during the fourth quarter of 2002. The other PLP that has been participating in the negotiations has filed for bankruptcy; however, the bankruptcy court has permitted the disbursement of funds related this environmental matter. It is currently expected that the actual cleanup of PCB sediments in the Spokane River will be coordinated to the extent possible with the EPA's separate plan to remove heavy metals from the Spokane River, contamination that resulted from decades of mining upstream at locations in Idaho and is not related to the activities of Avista Development.

Lake Coeur d'Alene

In July 1998, the United States District Court for the District of Idaho issued its finding that the Coeur d'Alene Tribe of Idaho owns portions of the bed and banks of Lake Coeur d'Alene and the St. Joe River lying within the current boundaries of the Coeur d'Alene Reservation. This action was brought by the United States on behalf of the Tribe against the State of Idaho. While the Company is not a party to this action, the Company is continuing to evaluate the potential impact of this decision on the operation of its hydroelectric facilities on the Spokane River, downstream of Lake Coeur d'Alene. The United States District Court decision was affirmed by the United States Court of Appeals for the Ninth Circuit. The United States Supreme Court affirmed this decision in June 2001. This will result in the Company being liable to the Coeur d'Alene Tribe of Idaho for payments for use of reservation lands under Section 10(e) of the Federal Power Act.

Spokane River Relicensing

The Company operates six hydroelectric plants on the Spokane River, and five of these (Long Lake, Nine Mile, Upper Falls, Monroe Street and Post Falls) are under one FERC license and referred to herein as the Spokane River Project. The sixth, Little Falls, is operated under separate Congressional authority and is not licensed by the FERC. The license for the Spokane River Project expires in August 2007; the Company filed a Notice of Intent to Relicense on July 29, 2002. The formal consultation process involving planning and information gathering with stakeholder groups is underway. The Company's goal is to develop with the stakeholders a comprehensive and cost-effective settlement agreement to be filed as part of the Company's license application to the FERC in July 2005.

Clark Fork Settlement Agreement

The issue of high levels of dissolved gas which exceed Idaho and federal water quality standards downstream of the Cabinet Gorge Hydroelectric Generating Project (Cabinet Gorge) during spill periods continues to be studied, as agreed to in the Clark Fork Settlement Agreement and incorporated into the renewed FERC license. To date, intensive biological studies in the lower Clark Fork River and Lake Pend Oreille have documented minimal biological effects of high dissolved gas levels on free ranging fish. Under the terms of the Clark Fork Settlement Agreement, the Company developed an abatement and mitigation strategy during 2002 with the other signatories to the agreement. In December 2002, the Company submitted its plan for review and approval by the other signatories as well as the FERC. The structural alternative proposed in the plan provides for the modification of the two existing diversion tunnels built when Cabinet Gorge was originally constructed. The costs of modifications to the first tunnel are currently estimated to be $37 million (including AFUDC and inflation) and would be incurred between 2004 and 2009. The second tunnel would be modified only after evaluation of the performance of the first tunnel and such modifications would commence no later than 10 years following the completion of the first tunnel. It is currently estimated that the costs to modify the second tunnel would be $23 million (including AFUDC and inflation). As part of the plan, the Company will also provide $0.5 million annually commencing as early as 2004, as mitigation for aquatic resources that might be adversely affected by high dissolved gas levels. Mitigation funds will continue until the modification of the second tunnel commences or if the second tunnel is not modified to an agreed upon point in time commensurate with the biological effects of high dissolved gas levels. The Company will seek regulatory recovery of the costs for the modification of Cabinet Gorge and the mitigation payments.

The operating license for the Clark Fork Projects describes the approach to restore bull trout populations in the project areas. Using the concept of adaptive management, the Company is evaluating the feasibility of fish passage and, depending upon the results of these experimental studies, determining the applications of funds toward continuing fish passage efforts or other population enhancement measures.

Other Contingencies

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

The Company routinely assesses, based on in-depth studies, expert analyses and legal reviews, its contingencies, obligations and commitments for remediation of contaminated sites, including assessments of ranges and probabilities of recoveries from other responsible parties who have and have not agreed to a settlement and recoveries from insurance carriers. The Company's policy is to immediately accrue and charge to current expense identified exposures related to environmental remediation sites based on estimates of investigation, cleanup and monitoring costs to be incurred.

The Company has potential liabilities under the Federal Endangered Species Act (ESA) for species of fish that have either already been added to the endangered species list, been listed as "threatened" or been petitioned for listing. Thus far, measures adopted and implemented have had minimal impact on the Company.

Under the federal licenses for its hydroelectric projects, the Company is obligated to protect its property rights, including water rights. The State of Montana is examining the status of all water right claims within state boundaries, which could potentially adversely affect the energy production of the Company's Cabinet Gorge and Noxon Rapids hydroelectric facilities. The Company is participating in this extended process, which is unlikely to be concluded in the foreseeable future.

The Company must be in compliance with requirements under the Clean Air Act Amendments (CAAA) at the Colstrip thermal generating plant, in which the Company maintains an ownership interest. The anticipated share of costs at Colstrip is not expected to have a major economic impact on the Company.

As of December 31, 2002, the Company's collective bargaining agreement with the International Brotherhood of Electrical Workers represented approximately 48 percent of all Avista Utilities employees. The current agreement with the local union representing the majority of the bargaining unit employees expires on March 25, 2005. A local agreement in the South Lake Tahoe area, which represents 5 employees, also expires on March 25, 2005. Three other labor agreements in Oregon, which cover approximately 55 employees, expire on March 31, 2003. Negotiations are currently ongoing with respect to the agreements that expire on March 31, 2003.

NOTE 29. DISPOSITION OF POWER PLANT

In May 2000, the owners of Centralia sold the plant to TransAlta. Avista Utilities recorded an after-tax gain totaling $37.2 million from the sale of its 17.5 percent ownership interest in the plant. Of the total after-tax gain, $9.0 million was recorded in the Consolidated Statements of Income and Comprehensive Income for the year ended December 31, 2000 and $28.2 million was deferred and returned to Avista Utilities' customers through rates over established periods of time. Washington customers received $20.7 million of the after-tax gain through pre-tax credits to their electric bills over the two-month period of December 2000 and January 2001. Idaho customers are receiving the remaining $7.5 million of the after-tax gain, which is a rate reduction of 1.8 percent, over an eight-year period.

NOTE 30. SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

The Company's energy operations are significantly affected by weather conditions. Consequently, there can be large variances in revenues, expenses and net income between quarters based on seasonal factors such as temperatures and streamflow conditions. A summary of quarterly operations (in thousands, except per share amounts) for 2002 and 2001 follows:

	Three Months Ended			
	March 31	June 30	September 30	December 31
2002				
Operating revenues	$306,979	$218,362	$189,830	$265,275
Operating expenses	260,471	180,627	169,453	225,208
Income from operations	46,508	37,735	20,377	40,067
Income (loss) from continuing operations	15,520	9,331	(1,082)	10,541
Income (loss) from discontinued operations	(272)	1,014	(533)	936
Net income before cumulative effect of accounting change	15,248	10,345	(1,615)	11,477
Cumulative effect of accounting change	(4,148)	-	-	-
Net income (loss)	11,100	10,345	(1,615)	11,477
Income (loss) available for common stock	$10,492	$9,737	$(2,223)	$10,899
Outstanding common stock:				
Weighted average	47,671	47,774	47,866	47,978
End of period	47,737	47,830	47,930	48,044
Earnings (loss) per share, basic and diluted:				
Earnings (loss) per share from continuing operations	$0.32	$0.18	$(0.04)	$0.21
Earnings (loss) per share from discontinued operations	(0.01)	0.02	(0.01)	0.02
Earnings (loss per share before cumulative effect of accounting change	0.31	0.20	(0.05)	0.23
Cumulative effect of accounting change	(0.09)	-	-	-
Total earnings (loss) per share, basic	$0.22	$0.20	$(0.05)	$0.23
Dividends paid per common share	$0.12	$0.12	$0.12	$0.12
Trading price range per common share:				
High	$16.47	$16.60	$13.89	$12.10
Low	$13.00	$11.00	$10.16	$8.75
2001				
Operating revenues	$473,855	$371,135	$232,113	$318,210
Operating expenses	408,408	314,585	198,494	304,534
Income from operations	65,447	56,550	33,619	13,676
Income (loss) from continuing operations	32,121	25,980	6,111	(4,607)
Loss from discontinued operations	(2,718)	(3,255)	(38,421)	(3,055)
Net income (loss)	29,403	22,725	(32,310)	(7,662)
Income (loss) available for common stock	$28,795	$22,117	$(32,918)	$(8,270)
Outstanding common stock:				
Weighted average	47,237	47,372	47,486	47,569
End of period	47,266	47,465	47,537	47,633
Earnings (loss) per share, basic and diluted:				
Earnings (loss) per share from continuing operations	$0.67	$0.54	$0.12	$(0.11)
Loss per share from discontinued operations	(0.06)	(0.07)	(0.81)	(0.06)
Total earnings (loss) per share, basic	$0.61	$0.47	$(0.69)	$(0.17)
Dividends paid per common share	$0.12	$0.12	$0.12	$0.12
Trading price range per common share:				
High	$20.63	$23.97	$19.98	$14.60
Low	$15.60	$16.27	$13.40	$10.60

INDEPENDENT AUDITORS' REPORT

Avista Corporation
Spokane, Washington

We have audited the accompanying consolidated balance sheets and statements of capitalization of Avista Corporation and subsidiaries (the Company) as of December 31, 2002 and 2001, and the related consolidated statements of income and comprehensive income, stockholders' equity, and cash flows, which include the schedule of information by business segments, for each of the three years in the period ended December 31, 2002. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2002 and 2001, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2 to the consolidated financial statements, during 2002, the Company changed its method of accounting for goodwill to conform to Statement of Financial Accounting Standards No. 142, also, as described in Note 2 to the consolidated financial statements, the Company changed its presentation of energy trading activities in accordance with Emerging Issues Task Force Issue No. 02-3.

Deloitte + Touche LLP

Seattle, Washington
February 7, 2003
(March 3, 2003, as to Note 28)

MANAGEMENT'S STATEMENT OF RESPONSIBILITY

Management of Avista Corporation is responsible for the accuracy and completeness of the information in this annual report. The financial and operating information presented is derived from company records and other sources. Certain amounts are, of necessity, based on judgment and estimation. Quality control practices for reporting business information in combination with the company's internal control procedures provide adequate assurance that the annual report fairly and reasonably presents the company's financial position and operating results.

The board of directors appointed Deloitte & Touche LLP, an independent accounting firm, to audit the consolidated financial statements. Deloitte & Touche LLP was provided access to all information and documentation necessary for the audit. Deloitte & Touche LLP's report follows the notes to the consolidated financial statements. In the course of their work, the independent auditors and internal auditors may recommend changes in control procedures. Management takes appropriate action based on such recommendations.

Gary G. Ely
Chairman, President and
Chief Executive Officer

Malyn K. Malquist
Senior Vice President and
Chief Financial Officer

SELECTED FINANCIAL DATA

	2002	2001	2000	1999	1998	1992
INCOME STATEMENT						
Operating revenues	$980,446	$1,395,313	$1,858,516	$1,222,274	$1,330,637	$557,758
Operating expenses	835,759	1,226,021	1,641,428	1,186,881	1,157,604	407,133
Income from operations	144,687	169,292	217,088	35,393	173,033	150,625
Interest expense	105,336	106,480	68,255	64,747	69,017	53,541
Income taxes	29,994	34,386	76,998	16,897	43,430	41,330
Income from continuing operations	34,310	59,605	101,055	28,662	78,316	72,267
Income (loss) from discontinued operations	1,145	(47,449)	(9,376)	(2,631)	(177)	2,403
Net income before cumulative effect of accounting change	35,455	12,156	91,679	26,031	78,139	74,670
Cumulative effect of accounting change	(4,148)	-	-	-	-	-
Net income	31,307	12,156	91,679	26,031	78,139	74,670
Preferred stock dividend requirements	2,402	2,432	23,735	21,392	8,399	6,817
Income available for common stock	28,905	9,724	67,944	4,639	69,740	67,853
Earnings per share, diluted:						
Avista Utilities	$0.71	$0.46	$(1.37)	$1.00	$0.88	$1.15
Energy Trading and Marketing	0.47	1.33	3.51	(1.59)	0.26	-
Information and Technology	(0.25)	(0.41)	(0.41)	(0.16)	(0.06)	-
Other	(0.26)	(0.18)	(0.06)	0.94	0.20	0.17
Earnings per share from continuing operations	$0.67	$1.20	$1.67	$0.19	$1.28	$1.32
Earnings (loss) per share from discontinued operations	0.02	(1.00)	(0.20)	(0.07)	0.00	0.05
Earnings per share before cumulative effect of accounting change	0.69	0.20	1.47	0.12	1.28	1.37
Loss per share from cumulative effect of accounting change	(0.09)	-	-	-	-	-
Total earnings per share, diluted	$0.60	$0.20	$1.47	$0.12	$1.28	$1.37
Total earnings per share, basic	$0.60	$0.21	$1.49	$0.12	$1.28	$1.37
COMMON STOCK STATISTICS						
Dividends paid per common share	$0.48	$0.48	$0.48	$0.48	$1.05	$1.24
Book value per common share	$14.84	$15.12	$15.34	$11.04	$12.07	$11.54
Shares of common stock:						
Outstanding	48,044	47,633	47,209	35,648	40,454	50,888
Average	47,823	47,417	45,690	38,213	54,604	49,550
Return on average common equity:						
Total company	4.0%	1.3%	12.9%	1.1%	11.3%	12.1%
Utility only	8.2%	5.9%	-23.7%	20.0%	12.7%	11.8%
Non-utility only	-1.7%	-3.4%	44.1%	-13.3%	9.1%	14.1%
Common stock price:						
High	$16.47	$23.97	$68.00	$19.56	$24.88	$18.38
Low	$8.75	$10.60	$14.63	$14.63	$16.25	$15.94
Year-end close	$11.56	$13.26	$20.50	$15.44	$19.25	$17.63
DEBT AND PREFERRED STOCK STATISTICS						
Pretax interest coverage:						
Including AFUDC/AFUCE	1.59(x)	1.32(x)	2.35(x)	1.97(x)	2.72(x)	3.10(x)
Excluding AFUDC/AFUCE	1.57(x)	1.29(x)	2.32(x)	1.93(x)	2.67(x)	3.03(x)
Embedded cost of debt	8.88%	8.78%	7.40%	6.95%	7.62%	8.88%
Embedded cost of preferred stock	7.42%	7.39%	7.39%	7.39%	7.21%	6.90%
Credit Ratings (S&P/Moody's)						
First Mortgage Bonds	BBB-/Baa3	BBB-/Baa3	BBB/Baa1	BBB+/A3	A/A3	A-/A3
Unsecured medium-term notes	BB+/Ba1	BB+/Ba1	BBB/Baa2	BBB/Baa1	A-/Baa1	BBB+/Baa1
Preferred stock	BB-/Ba3	BB-/Ba3	BBB/Baa3	BBB/Baa2	A-/Baa1	BBB+/baa1
OTHER FINANCIAL AND OPERATING STATISTICS						
Total assets	$3,614,133	$4,037,223	$12,577,081	$3,713,494	$3,253,636	$1,534,015
Total net utility property	1,563,704	1,565,642	1,518,312	1,500,837	1,470,942	1,191,153
Utility capital expenditures	64,207	119,905	98,680	87,160	92,295	97,707
Total capitalization:						
Long-term debt	902,635	$1,175,715	$679,806	$714,904	$730,022	$596,897
Preferred trust securities	100,000	100,000	100,000	110,000	110,000	-
Preferred stock	33,250	35,000	35,000	35,000	35,000	135,000
Convertible preferred stock	-	-	-	263,309	269,227	-
Common equity	712,791	720,063	724,224	393,499	488,034	587,035
Total	$1,748,676	$2,030,778	$1,539,030	$1,516,712	$1,632,283	$1,318,932
Capitalization Ratios:						
Long-term debt	51.62%	57.89%	44.17%	47.14%	44.72%	45.26%
Preferred securities	7.62%	6.65%	8.77%	26.92%	25.38%	10.23%
Common equity	40.76%	35.46%	47.06%	25.94%	29.90%	44.51%
Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%

SELECTED FINANCIAL DATA

	2002	2001	2000	1999	1998	1992
AVISTA UTILITIES						
Electric Operations						
Electric revenues (millions of dollars):						
Residential	$196.1	$158.8	$158.1	$158.6	$157.0	$146.1
Commercial	194.7	155.4	149.8	152.1	149.8	121.3
Industrial	68.1	80.4	83.0	69.6	64.6	50.9
Public street and highway lighting	4.7	3.8	3.6	3.5	3.4	2.9
Total retail revenues	463.6	398.4	394.5	383.8	374.8	321.2
Wholesale revenues	64.1	480.9	864.7	522.5	457.3	91.8
Other revenues	56.4	42.9	28.1	21.9	24.0	11.4
Total electric revenues	$584.1	$922.2	$1,287.3	$928.2	$856.1	$424.4
Electric energy sales (millions of kWhs):						
Residential	3,202.9	3,219.4	3,279.4	3,237.4	3,217.1	3,023.9
Commercial	2,836.7	2,882.0	2,885.8	2,848.1	2,810.2	2,298.5
Industrial	1,519.1	1,891.2	2,047.9	2,032.3	1,878.4	1,562.5
Public street and highway lighting	25.2	25.0	24.7	24.7	23.8	20.5
Total electric retail sales	7,583.9	8,017.6	8,237.8	8,142.5	7,929.5	6,905.4
Wholesale energy sales	2,215.5	6,261.6	15,806.7	19,777.8	19,214.8	3,162.4
Total electric energy sales	9,799.4	14,279.2	24,044.5	27,920.3	27,144.3	10,067.8
Electric customers (average per year):						
Residential	279,735	276,845	273,219	270,013	265,891	227,575
Commercial	35,910	35,454	35,060	34,877	34,407	27,781
Industrial	1,420	1,434	1,254	1,189	1,169	974
Public street and highway lighting	413	402	392	389	383	302
Total electric retail customers	317,478	314,135	309,925	306,468	301,850	256,632
Wholesale	46	44	58	68	85	26
Total electric customers	317,524	314,179	309,983	306,536	301,935	256,658
Electric customers (at year-end):						
Residential	282,269	279,129	276,382	272,342	269,101	230,579
Commercial	36,106	35,726	35,109	35,197	34,708	28,105
Industrial	1,409	1,424	1,398	1,078	1,003	906
Public street and highway lighting	426	415	401	395	399	302
Total retail electric customers	320,210	316,694	313,290	309,012	305,211	259,892
Wholesale	50	32	51	65	67	25
Total electric customers	320,260	316,726	313,341	309,077	305,278	259,917
Revenue per residential kWh (cents)	6.12	4.93	4.82	4.90	4.88	4.83
Use per residential customer (kWh)	11,450	11,629	12,003	11,990	12,099	13,287
Revenue per commercial kWh (cents)	6.86	5.39	5.19	5.34	5.33	5.28
Use per commercial customer (kWh)	78,995	81,288	82,311	81,662	81,676	82,737
Electric energy resources (millions of kWhs):						
Hydro generation (Company facilities)	4,009.6	2,563.8	3,818.7	4,286.4	3,860.2	2,969.5
Thermal generation (Company facilities)	1,714.3	3,000.7	3,153.6	3,353.2	3,521.6	3,310.5
Purchased power - long-term hydro	836.6	631.4	928.6	1,093.1	909.6	1,275.8
Purchased power - other	3,827.8	8,623.7	16,705.8	19,696.5	19,405.4	2,974.5
Power exchanges	13.4	(103.7)	67.2	16.3	26.0	71.7
Total power resources	10,401.7	14,715.9	24,673.9	28,445.5	27,722.8	10,602.0
Energy losses and company use	(602.3)	(436.7)	(629.4)	(525.2)	(578.5)	(534.2)
Total electric energy resources	9,799.4	14,279.2	24,044.5	27,920.3	27,144.3	10,067.8

SELECTED FINANCIAL DATA

Electric Operations (continued)	2002	2001	2000	1999	1998	1992
Total resources available at peak (MW):						
Company owned:						
Hydro	955	956	956	956	956	955
Thermal	426	462	586	685	705	530
Purchased power:						
Long-term hydro	159	144	184	180	192	206
Other	673	1,991	2,468	3,010	3,138	589
Total resources available at peak	2,213	3,553	4,194	4,831	4,991	2,280
Net system peak demand (winter)	1,346	1,500	1,491	1,421	1,701	1,493
Wholesale obligations	297	1,734	2,338	3,211	3,064	525
Total requirements (winter)	1,643	3,234	3,829	4,632	4,765	2,018
Reserve margin	26%	9%	9%	4%	5%	13%
Annual load factor	62%	65%	68%	70%	64%	59%
Average cost of production (cents per kWh)	2.30	3.41	2.70	2.22	2.34	2.64
Natural Gas Operations						
Natural gas revenues (millions of dollars):						
Residential	$184.0	$179.6	$128.2	$99.9	$92.6	$48.4
Commercial	105.0	104.0	70.0	51.9	49.6	32.0
Industrial	7.1	11.2	7.7	5.1	5.3	7.7
Total retail revenues	296.1	294.8	205.9	156.9	147.5	88.1
Wholesale revenues	0.7	1.8	5.7	15.2	24.8	-
Transportation revenues	9.6	8.6	10.2	10.8	12.1	8.6
Other revenues	3.4	3.4	3.0	4.6	8.7	3.9
Total natural gas revenues	$309.8	$308.6	$224.8	$187.5	$193.1	$100.6
Natural gas sales (millions of therms):						
Residential	199.7	198.4	212.2	200.2	187.6	117.7
Commercial	126.2	126.9	135.1	125.6	122.3	95.6
Industrial	11.3	15.5	18.3	16.4	17.5	28.2
Total retail sales	337.2	340.8	365.6	342.2	327.4	241.5
Transportation and other	179.3	201.2	230.3	316.7	385.3	181.5
Total natural gas therm sales	516.5	542.0	595.9	658.9	712.7	423.0
Natural gas customers (average per year):						
Residential	254,700	249,650	242,983	234,844	226,165	148,242
Commercial	30,823	30,355	29,739	29,032	28,236	21,816
Industrial	315	328	334	338	336	295
Total retail customers	285,838	280,333	273,056	264,214	254,737	170,353
Transportation and other	89	88	98	116	138	60
Total natural gas customers	285,927	280,421	273,154	264,330	254,875	170,413
Natural gas customers (at year-end):						
Residential	258,738	253,325	248,418	239,321	233,017	155,495
Commercial	31,141	30,697	30,138	29,432	28,770	22,264
Industrial	309	318	332	332	332	299
Total retail customers	290,188	284,340	278,888	269,085	262,119	178,058
Transportation and other	90	82	96	129	163	92
Total natural gas customers	290,278	284,422	278,984	269,214	262,282	178,150

SELECTED FINANCIAL DATA

	2002	2001	2000	1999	1998	1992
Natural Gas Operations (continued)						
Revenue per residential therm (cents)	92.13	90.51	60.43	49.89	49.38	41.13
Use per residential customer (therms)	784	795	873	852	829	794
Revenue per commercial therm (cents)	83.17	81.98	51.79	41.36	40.52	33.45
Use per commercial customer (therms)	4,095	4,180	4,544	4,327	4,330	4,383
Heating degree days (at Spokane, Washington):						
Actual	6,818	6,800	7,176	6,408	5,951	6,134
30 year average	6,842	6,842	6,842	6,842	6,842	6,882
Actual as a percent of average	100%	99%	105%	94%	87%	89%
ENERGY TRADING AND MARKETING						
Gross Realized Sales Transactions (millions of dollars)						
Electric	$1,417.5	$3,380.1	$4,721.3	$4,745.6	$1,665.3	$ -
Natural gas	958.2	1,619.3	1,751.3	1,900.5	743.4	-
Other	-	1.6	59.0	49.6	-	-
Total revenues	$2,375.7	$5,001.0	$6,531.6	$6,695.7	$2,408.7	$ -
Gross Realized Sales Volume						
Electricity (thousands of MWhs)	40,426	47,927	105,548	135,099	54,430	-
Natural gas (thousands of dekatherms)	225,983	248,193	273,448	775,822	424,152	-
Coal (thousands of tons)	-	-	3,514	1,638	-	-
Total assets (millions of dollars)	$1,349.6	$1,506.2	$10,271.8	$1,595.5	$955.6	$ -
INFORMATION AND TECHNOLOGY						
Revenues (millions of dollars)	$17.6	$13.8	$5.7	$2.3	$1.3	$ -
Total assets (millions of dollars)	$37.5	$26.9	$14.4	$6.3	$2.5	$ -
OTHER OPERATING RESULTS						
Revenues (millions of dollars)	$14.6	$16.4	$32.9	$122.3	$231.5	$32.8
Total assets (millions of dollars)	$42.9	$86.5	$96.4	$114.9	$285.6	$109.2

Energy Trading and Marketing – Energy Trading and Marketing's net income was $22.4 million for 2002, compared to $63.2 million for 2001. The primary reason for the decrease in net income was a decrease in the net margin on energy trading activities. Net margin on energy trading activities, which is reported as operating revenues, was $54.2 million for 2002 compared to $134.3 million for 2001. Realized gains decreased to $141.6 million for 2002 from $164.5 million for 2001. Realized gains represent the net gain on contracts that have settled. The decrease was primarily due to a decrease in the underlying commodity values that settled and a decrease in the volume of transactions. The decrease in the volume of transactions was primarily due to reduced liquidity in wholesale markets, fewer creditworthy counterparties participating in the wholesale markets and a decrease in the volatility of prices in the wholesale markets. The total mark-to-market adjustment for Energy Trading and Marketing was an unrealized loss of $87.4 million for 2002 compared to an unrealized loss of $30.2 million for 2001. The increase in the unrealized loss is primarily due to the settlement of contracts and the realization of previously unrealized gains and decreased volatility in the wholesale energy markets.

Information and Technology – Information and Technology's net loss was $12.1 million for 2002 compared to $19.4 million for 2001. Operating revenues for this line of business increased $3.8 million and operating expenses decreased $7.2 million, as compared to 2001. Avista Advantage accounted for the increase in revenues primarily due to the expansion of its customer base. The decrease in operating expenses reflects reduced expenses for Avista Advantage and Avista Labs due to improved efficiencies, a reduction in the number of employees and a focus on reducing operating expenses.

Other – The net loss before cumulative effect of accounting change from this line of business was $12.4 million for 2002, compared to $8.4 million for 2001. The increase in the net loss was primarily due to a decrease in income from operations and partially due to an increase in interest expense as well as a reduction in gains on the disposition of assets. Operating revenues from this line of business decreased $1.7 million and operating expenses increased $2.7 million, respectively, for 2002 as compared to 2001. The decrease in income from operations was primarily due to an increase in litigation costs and settlements as well as an increase in the loss from other subsidiary operations.

Discontinued Operations – In September 2001, the Company reached a decision that it would dispose of substantially all of the assets of Avista Communications. The divestiture of operating assets was complete by the end of 2002. Certain liabilities of the operations remain to be settled. Net income for 2002 was $1.1 million, compared to a net loss of $47.4 million for 2001. Net income for 2002 was primarily due to the settlement of contracts and liabilities during the period as well as the favorable settlement of a lawsuit during the period. The significant net loss for 2001 was due to asset impairment charges of $58.4 million recorded during the third quarter of 2001.

Capitalization – During 2002, short-term borrowings decreased $45.1 million and the Company repurchased $203.6 million of long-term debt scheduled to mature in future years. The overall decrease in borrowings during 2002 reflects increased cash flows from operations primarily related to the recovery of deferred power and natural gas costs as well as a general rate increase for Washington electric customers that was partially used to repurchase long-term debt. Cash dividends from Avista Energy were also a significant source of funds used to repurchase long-term debt during 2002.

The Company's consolidated capital structure, including the current portion of long-term debt and short-term borrowings was 54.3 percent debt, 5.4 percent preferred trust securities, 1.8 percent preferred stock, and 38.5 percent common equity, as of December 31, 2002, compared to 59.4 percent debt, 4.7 percent preferred trust securities, 1.7 percent preferred stock, and 34.2 percent common equity as of December 31, 2001. The Company has a target capital structure of 50 percent debt and 50 percent preferred trust securities, preferred stock and common equity. The Company plans to achieve this capital structure primarily with the reduction of total debt and the retention of net earnings.

Pension Plan – As of December 31, 2002, the Company's pension plan had assets with a fair value that was less than the present value of the accumulated benefit obligation under the plan. In 2002, the Company recorded an additional minimum liability for the unfunded accumulated benefit obligation of $33.4 million and an intangible asset of $6.4 million related to the pension plan. This resulted in a charge to other comprehensive income of $17.6 million, net of taxes. The Company does not expect the current pension plan funding deficit to have a material adverse impact on its financial condition, results of operations or cash flows. The Company made $12 million in cash contributions to the pension plan in 2002 and the Company's funding contribution is expected to be approximately $12 million for 2003.

Off-balance Sheet Arrangements – Avista Receivables Corp. (ARC) was formed for the purpose of acquiring or purchasing interests in certain accounts receivable, both billed and unbilled, of the Company. Under the current agreement that expires in May 2005, ARC can sell without recourse, on a revolving basis, up to $100.0 million of those receivables. As of December 31, 2002, $65.0 million in receivables were sold pursuant to the agreement.

WP Funding LP is an entity that was formed for the purpose of acquiring the natural gas-fired combustion turbine generating facility in Rathdrum, Idaho (Rathdrum CT). WP Funding LP purchased the Rathdrum CT from the Company with funds provided by unrelated investors of which 97 percent represented debt and 3 percent represented equity. The Company operates the Rathdrum CT and leases it from WP Funding LP and currently makes lease payments of $4.5 million per year. The total amount of WP Funding LP debt outstanding that is not included on the Company's consolidated balance sheet was $54.5 million as of December 31, 2002. A recent interpretation issued by the Financial Accounting Standards Board will require the Company to begin consolidating WP Funding LP into its financial statements effective July 1, 2003, whereby the debt outstanding and the book value of the Rathdrum CT will be included in the Company's consolidated balance sheet.

BOARD OF DIRECTORS

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Kirkland, Washington
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Kristianne Gates Blake, P.S.
Spokane, Washington
Director since 2000

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Managing Director
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President
Lura J. Powell & Associates
Richland, Washington
Director since 2003

R. John Taylor
Chairman and Chief
Executive Officer
AIA Services Corporation
Lewiston, Idaho
Director since 1985

TRIBUTE

Sarah M.R. (Sally) Jewell
Executive Vice President and Chief Operating Officer
Recreational Equipment, Inc. (REI)
Kirkland, Washington
Director since 1997

Following six years of dedication to Avista, Sally Jewell will complete her service as a board member at the company's annual meeting in May 2003. We've been enriched over the years by Sally's invaluable strategic and financial expertise, her thoughtful perspective and endless enthusiasm. Sally will be greatly missed by her fellow board members and Avista colleagues.

Bobby Schmidt
President
Schmidt Trading, Inc.,
Hilton Head Island, South Carolina
Director since 1997

Bob left the board on May 28, 2002, after serving as a board member for five dedicated years. We benefited tremendously from his energy trading expertise, wealth of knowledge and wise counsel. We are grateful for Bob's commitment and support, and wish him our best as he continues to be engaged in his many and diverse endeavors.

CORPORATE AND BUSINESS UNIT OFFICERS

Corporate

Gary G. Ely
Chairman, President and
Chief Executive Officer

Malyn K. Malquist
Senior Vice President and
Chief Financial Officer

David J. Meyer
Senior Vice President and
General Counsel

Scott L. Morris
Senior Vice President

Terry L. Syms
Vice President and
Assistant to the
Chairman

David A. Brukardt
Vice President and
Treasurer

Christy M. Burmeister-Smith
Vice President and
Controller

Karen S. Feltes
Vice President of Human
Resources and Corporate
Secretary

Kelly O. Norwood
Vice President

Ronald R. Peterson
Vice President

Roger D. Woodworth
Vice President

Business Unit

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Harry E. Stephens
President and Chief
Executive Officer

Gerry D. Crooks
Founder and Chief
Strategic Officer

Avista Energy
Dennis P. Vermillion
President and Chief
Operating Officer

Avista Labs
J. Michael Davis
President and Chief
Executive Officer

Avista Utilities
Scott L. Morris
President

TRIBUTE

Jon E. Eliassen
For more than three decades, Jon has served Avista Corp., the industry and the community. He joined the company in 1970 and over the course of his tenure, Jon made a vital contribution as an invaluable member of our leadership team. He served as Avista's chief financial officer and in a number of other financial positions.

The boards of Western Energy Institute, Pacific Coast Gas Association, Edison Electric Institute, Western Electric Power Institute, the Spokane Symphony Endowment Fund, the Northwest Museum of Arts and Culture, and the Spokane Intercollegiate Research and Technology Institute have all benefited from Jon's insight and energy.

We wish Jon and his wife, Val, happiness in retirement.

CORPORATE INFORMATION

Company Headquarters

Avista Corp.
1411 East Mission Avenue
Spokane, Washington 99202

Avista Corp. on the Internet

Financial results, stock quotes, news releases, documents filed with the Securities and Exchange Commission and information on the company's products and services are available at Avista Corp.'s home page on the Internet. The address is http://www.avistacorp.com.

Transfer Agent

The Bank of New York is the company's stock transfer, dividend payment and reinvestment plan agent. Answers to many shareholder questions and requests for forms are available by visiting The Bank of New York's Web site at http://www.stockbny.com.

Inquiries should be directed to:

The Bank of New York
Shareholder Relations Department
P.O. Box 11258
Church Street Station
New York, New York 10286-1258
Phone: (800) 642-7365
e-mail: shareowner-svcs@bankofny.com

Investor Information

A copy of the company's financial reports, including the reports on Forms 10-K and 10-Q filed with the Securities and Exchange Commission, will be provided, without charge, upon request to:

Avista Corp.
Investor Relations
P.O. Box 3727 MSC-18
Spokane, Washington 99220-3727
Phone: (800) 222-4931

Annual Meeting of Shareholders

Shareholders are invited to attend the company's annual meeting to be held at 10 a.m. PDT on Thursday, May 8, 2003, at Avista Corp. headquarters, 1411 East Mission Avenue in Spokane, Washington.

The annual meeting also will be webcast. Please go to http://www.avistacorp.com to preregister for the webcast in advance of the annual meeting and to listen to the live webcast. The webcast will be archived at http://www.avistacorp.com through 5 p.m. PDT on May 15, 2003, to allow shareholders to listen to it at their convenience.

Exchange Listings

Ticker Symbol: AVA
New York Stock Exchange
Pacific Exchange

AVA LISTED NYSE

This annual report contains forward-looking statements regarding the company's current expectations. These statements are subject to a variety of risks and uncertainties that could cause actual results to differ materially from the expectations. These risks and uncertainties include, in addition to those discussed herein, all factors discussed in the company's annual report on Form 10-K for the year 2002. Our 2002 annual report is provided for investors. It is not intended for use in connection with any sale or purchase of or any solicitation of others to buy or sell securities.

Avista employees featured on the cover by row from left to right: TOP ROW – Tim Carlberg / Coyote Springs 2 Project Manager; Diane Thoren / Assistant Treasurer and Director of Corporate Finance; Don Falkner / Manager of Revenue Requirements. MIDDLE ROW – Arnette Daniels / Dispatcher; Jiong Ji / Senior Analyst; Malyn Malquist / Chief Financial Officer and Senior Vice President of Avista Corp. BOTTOM ROW – Scott Morris / Senior Vice President of Avista Corp. and President of Avista Utilities; Hassel Dotson / Line Foreman; Ann Carey / Associate Vice President of Sales.

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