

EL PASO ELECTRIC CO /TX/
Form 424B2
May 29, 2008

The information in this preliminary prospectus supplement is not complete and may be changed. A registration statement relating to these notes has been filed with the Securities Exchange Commission and is effective. This preliminary prospectus is not an offer to sell these notes and is not soliciting an offer to buy these notes in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED MAY 29, 2008

PROSPECTUS SUPPLEMENT TO PROSPECTUS DATED MAY 20, 2008

\$

El Paso Electric Company

% Senior Notes due

We will pay interest on the Senior Notes each March 15 and September 15. The first interest payment will be made on September 15, 2008.

We may redeem some or all of the Senior Notes at any time and from time to time at the make-whole redemption price described herein.

The Senior Notes will be our senior unsecured obligations and will rank equally with all our other existing and future senior unsecured debt from time to time outstanding.

Investing in the Senior Notes involves risks. See "Risk Factors" beginning on page S-4.

Price to(1)

| | | | | | | | |
|-----------------------------------|---------------------|---|---------|----|----|----|--|
| Public Underwriting | | | | | | | |
| Discounts and | | | | | | | |
| Commissions | Proceeds to El Paso | | | | | | |
| Electric Company | | | | | | | |
| (before expenses) Per Senior Note | % | % | % Total | \$ | \$ | \$ | |

(1) Plus

accrued interest from _____, 2008, if settlement occurs after that date.

Delivery of the Senior Notes in book-entry form only will be made on or about _____, 2008.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the prospectus to which it relates is truthful or complete. Any representation to the contrary is a criminal offense.

Credit Suisse

The date of this prospectus supplement is _____, 2008.

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You should rely only on the information incorporated by reference or provided in this prospectus supplement and the accompanying prospectus. No person has been authorized to give any information or to make any representation other than those set forth or incorporated by reference in this prospectus supplement and the accompanying prospectus and, if given or made, such information or representations must not be relied upon. We are not, and the underwriter is not, making an offer of these securities in any jurisdiction where the offer is not permitted. You should not assume that the information in this prospectus supplement and the accompanying prospectus is accurate as of any date other than the date on the front of this prospectus supplement or that the documents incorporated by reference are accurate as of any date other than the date that those documents were filed by us with the Securities and Exchange Commission.

All references to “El Paso”, “the Company”, “we”, “us,” “the Registrant,” “our,” or similar words are to El Paso Electric and, except as expressly stated or the context otherwise requires, not to any of its subsidiaries.

Summary

The following summary information is qualified in its entirety by the information contained elsewhere in this prospectus supplement and the accompanying prospectus, including the documents we have incorporated by reference, and in the indenture as described under “Description of the Senior Notes.” You should read the prospectus supplement, accompanying prospectus and the documents incorporated by reference in their entirety. This prospectus supplement and the accompanying prospectus contain or incorporate certain forward-looking statements. Forward-looking statements should be read together with the cautionary statements and factors referred to under “Special Note on Forward-Looking Statements” in the accompanying prospectus.

The Company

El Paso Electric Company is a public utility engaged in the generation, transmission and distribution of electricity in an area of approximately 10,000 square miles in west Texas and southern New Mexico. We also serve a wholesale customer in Texas and from time to time a customer in the Republic of Mexico. We own or have significant ownership interests in six electrical generating facilities providing us with a net dependable generating capability of 1,503 MW. For the year ended December 31, 2007, our energy sources consisted of approximately 43% nuclear fuel, 28% natural gas, 7% coal, 22% purchased power and less than 1% generated by wind turbines.

We serve approximately 360,000 residential, commercial, industrial and wholesale customers. We distribute electricity to retail customers principally in El Paso, Texas and Las Cruces, New Mexico (representing approximately 55% and 9%, respectively, of our operating revenues for the year ended December 31, 2007). In addition, our wholesale sales include sales for resale to other electric utilities and power marketers. Our principal industrial and other large customers include United States military installations, including Fort Bliss in Texas and White Sands Missile Range and Holloman Air Force Base in New Mexico, two large universities, and oil, copper refining and steel production facilities.

We were incorporated in Texas in 1901. As of January 31, 2008, we had approximately 1,000 employees, 44% of whom are covered by a collective bargaining agreement.

Our principal offices are located at the Stanton Tower, 100 North Stanton, El Paso, Texas 79901 (telephone 915-543-5711). The Company makes available free of charge through its website, www.epelectric.com, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission (“SEC”). Information contained on our website is not part of this prospectus supplement or the accompanying prospectus.

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The Offering

Issuer El Paso Electric Company, a Texas corporation.

Securities Offered \$ aggregate principal amount of % Senior Notes due .

Maturity March 15, .

Interest Payment Dates March 15 and September 15 of each year, commencing on September 15, 2008.

Interest Rate % per year.

Further Issuances We may issue additional debt securities under the indenture relating to the Senior Notes having the same terms and CUSIP number as the Senior Notes in all respects, except for the issue date and the issue price. Any such additional debt securities will be consolidated with and form a single series with the Senior Notes offered hereby.

In addition to the Senior Notes, we may issue other series of debt securities under the indenture relating to the Senior Notes. There is no limit on the total aggregate principal amount of debt securities that we can issue under the indenture relating to the Senior Notes.

Covenants The Senior Notes will be subject to covenants that will limit our ability to:

- Create liens on our operating property; and

Consolidate with or merge into, or transfer all or substantially all of our assets to any other party.

These covenants are subject to important exceptions and qualifications that are described under “Description of Debt Securities — Successor Obligor” in the accompanying prospectus and under “Description of the Senior Notes — Limitation on Liens.”

Events of Default The Senior Notes will be subject to the events of default described under “Description of Debt Securities — Defaults and Remedies” in the accompanying prospectus.

In addition, it will be an event of default under the Senior Notes if we fail to observe or perform any term, covenant, condition or agreement contained in any agreement or instrument evidencing or governing any indebtedness of the Company in a principal amount in excess of \$10,000,000 if the effect of any such failure is to cause such indebtedness to become due prior to its maturity. See “Description of the Senior Notes — Events of Default.”

Optional Redemption We may redeem the Senior Notes, in whole or in part, at any time and from time to time, at the make-whole redemption price described under “Description of the Senior Notes — Optional Redemption.”

Ranking
The Senior Notes will be our senior unsecured obligations and will rank equally with all our other existing and future senior unsecured debt, including all other debt securities issued under the indenture relating to the Senior Notes, from time to time outstanding. See “Description of Debt Securities — Ranking” in the accompanying prospectus.

Form and Denomination The Senior Notes will be issued in fully registered form in denominations of \$2,000 and in integral multiples of \$1,000 thereafter.

DTC Eligibility Senior Notes will be represented by global certificates deposited with, or on behalf of, The Depository Trust Company (DTC) or its nominee. See “Description of the Senior Notes — Book-Entry System.”

Same Day Settlement Beneficial interests in the Senior Notes will trade in DTC’s same-day funds settlement system until maturity. Therefore, secondary market trading activity in such interests will be settled in immediately available funds.

Use of Proceeds The net proceeds of this offering are intended to be used for general corporate purposes, which may include funding capital expenditures, repayment of debt and ensuring adequate liquidity. See “Use of Proceeds.”

Risk Factors See “Risk Factors” beginning on page S-4 of this prospectus supplement and other information included or incorporated by reference in this prospectus supplement and the accompanying prospectus for a discussion of factors you should carefully consider before investing in the Senior Notes.

Trustee The Bank of New York Trust Company, N.A.
Listing

The Senior Notes will not be listed on any national securities exchange.

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Risk Factors

Like other companies in our industry, our consolidated financial results will be impacted by weather, the economy of our service territory, fuel prices, the performance of our customers and the decisions of regulatory agencies. Our common stock price and creditworthiness will be affected by national and international macroeconomic trends, general market conditions and the expectations of the investment community, all of which are largely beyond our control. In addition, the following statements highlight risk factors that may affect our consolidated financial condition and results of operations. This is not intended to be an exhaustive discussion of all such risks, and the statements below must be read together with factors discussed elsewhere in this document and in our other filings with the SEC.

Risks Related to Our Business

Our Costs Could Increase or We Could Experience Reduced Revenues if There Are Problems at the Palo Verde Nuclear Generating Station

A significant percentage of our generating capacity, off-system sales margins, assets and operating expenses is attributable to the Palo Verde Nuclear Generating Station. Our 15.8% interest in each of the three Palo Verde units totals approximately 633 MW of generating capacity. Palo Verde represents approximately 42% of our available net generating capacity and represented approximately 43% of our available energy for the twelve months ended December 31, 2007. Palo Verde comprises 41% of our total net plant-in-service and Palo Verde expenses comprise a significant portion of operation and maintenance expenses. Arizona Public Service Company is the operating agent for Palo Verde, and we have limited ability under the Arizona Nuclear Power Project Participation Agreement to influence operations and costs at Palo Verde. Palo Verde operated at a capacity factor of 78.5% and 70.4% in the twelve months ended December 31, 2007 and 2006, respectively.

The Nuclear Regulatory Commission (“NRC”) has placed Palo Verde Unit 3 in the “multiple repetitive degraded cornerstone” column of its action matrix which results in an enhanced NRC inspection regimen. We face the risk of additional or unanticipated costs at Palo Verde resulting from (i) increases in operation and maintenance expenses, including additional costs relating to the enhanced NRC oversight; (ii) increases in the cost of uranium; (iii) the replacement of reactor vessel heads at the Palo Verde units; (iv) an extended outage of any of the Palo Verde units; (v) increases in estimates of decommissioning costs; (vi) the storage of radioactive waste, including spent nuclear fuel; (vii) prolonged reductions in generating output; (viii) insolvency of other Palo Verde Participants; and (ix) compliance with the various requirements and regulations governing commercial nuclear generating stations.

Our ability to increase retail base rates in Texas is limited through June 2010. We cannot seek approval to increase our base rates in Texas in the event of increases in non-fuel costs or loss of revenue unless our return on equity falls below the bottom of a defined range which currently is approximately 8.3%. Our rates in New Mexico will be fixed until after the conclusion of the May 2009 rate filing. We cannot assure that revenues will be sufficient to recover any increased costs, including any increased costs in connection with Palo Verde or other operations, whether as a result of inflation, changes in tax laws or regulatory requirements, or other causes.

We May Not Be Able to Recover All of Our Fuel Expenses from Customers

In general, by law, we are entitled to recover our prudently incurred fuel and purchased power expenses from our customers in Texas and New Mexico. The 2007 New Mexico Stipulation provides for energy from the deregulated Palo Verde Unit 3 to be recovered through fuel and purchased power costs based upon the contract cost of capacity and fuel for power purchased under the existing Southwestern Public Service Company (“SPS”) purchased power

contract. The 2007 New Mexico Stipulation requires the Company to file its Fuel and Purchased Power Cost Adjustment Clause (“FPPCAC”) according to New Mexico Public Regulation Commission (“NMPRC”) rules, at which time any party may propose to change the price of capacity and related energy from Palo Verde Unit 3 after the SPS purchased power contract is terminated September 30, 2009. The fuel expense in

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New Mexico and Texas is subject to reconciliation by the Public Utility Commission of Texas (“Texas Commission”) and the NMPRC. Prior to the completion of a reconciliation, we record fuel and purchased power costs transactions such that fuel revenues equal fuel and purchased power expense including the repriced energy costs for Palo Verde Unit 3 in New Mexico. In the event that a disallowance occurs during a reconciliation proceeding, the amounts recorded for fuel and purchased power expenses could differ from the amounts we are allowed to collect from our customers and we would incur a loss to the extent of the disallowance.

In New Mexico, the FPPCAC allows us to reflect current fuel and purchased power expenses in the FPPCAC and to adjust for under-recoveries and over-recoveries with a two-month lag. In Texas, fuel costs are recovered through a fixed fuel factor that may be adjusted two times per year. If we materially under-recover fuel costs, we may seek a surcharge to recover those costs at the time of the next fuel factor filing. During periods of significant increases in natural gas prices such as occurred in 2005, the Company realizes a lag in the ability to reflect increases in fuel costs in its fuel recovery mechanisms. As a result, cash flow is impacted due to the lag in payment of fuel costs and collection of fuel costs from customers. At December 31, 2007 and December 31, 2006, the Company had deferred fuel balances of \$27.7 million and \$32.6 million, respectively. To the extent the fuel and purchased power recovery processes in Texas and New Mexico do not provide for the timely recovery of such costs, we could experience a material negative impact on our cash flow.

Equipment Failures and Other External Factors Can Adversely Affect Our Results

The generation and transmission of electricity require the use of expensive and complex equipment. While we have a maintenance program in place, generating plants are subject to unplanned outages because of equipment failure. We are particularly vulnerable to this due to the advanced age of several of our gas-fired generating units in or near El Paso. In addition, we are seeking to extend the lives of these plants. In the event of unplanned outages, we must acquire power from others at unpredictable costs in order to supply our customers and comply with our contractual agreements. This can materially increase our costs and prevent us from selling excess power at wholesale, thus reducing our profits. In addition, actions of other utilities may adversely affect our ability to use transmission lines to deliver or import power, thus subjecting us to unexpected expenses or to the cost and uncertainty of public policy initiatives. We are particularly vulnerable to this because a significant portion of our available energy (at Palo Verde and the Four Corners Generating Station) is located hundreds of miles from El Paso and Las Cruces and must be delivered to our customers over long distance transmission lines. In addition, Palo Verde’s availability is an important factor in realizing off-system sales margins. These factors, as well as weather, interest rates, economic conditions, fuel prices and price volatility, are largely beyond our control, but may have a material adverse effect on our consolidated earnings, cash flows and financial position.

We May Not Be Able to Recover All Costs of New Generation

We have obtained from the Texas Commission and the NMPRC Certificates of Convenience and Necessity to construct a new generating unit (Newman Unit 5) in El Paso to meet our expected customers’ demand for electricity. We have provided the estimated cost of constructing Newman Unit 5 to the Texas Commission and NMPRC. We have risks associated with completing the construction of Newman Unit 5 on time and within projected costs. In addition, we have risks associated with obtaining financing for Newman Unit 5 at reasonable rates as we expect to issue debt to finance a portion of the plant.

The cost of financing and constructing Newman Unit 5 will be reviewed in future rate cases in both Texas and New Mexico. To the extent that the Texas Commission or NMPRC determines that the costs of construction are not reasonable because of cost overruns, delays or other reasons, we may not be allowed to recover these costs from

customers in base rates.

In addition, if the unit is not completed on time, we may be required to purchase power or operate less efficient generating units to meet customer requirements. Any replacement purchased power or fuel costs will be subject to regulatory review by the Texas Commission and NMPRC. We face financial risks to the extent that recovery is not allowed for any replacement fuel costs resulting from delays in the completion of Newman Unit 5.

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Competition and Deregulation Could Result in a Loss of Customers and Increased Costs

As a result of changes in federal law, our wholesale and large retail customers already have, in varying degrees, alternate sources of power, including co-generation of electric power. Deregulation legislation is in effect in Texas requiring us to separate our transmission and distribution functions, which would remain regulated, from our power generation and energy services businesses, which would operate in a competitive market, in the future. In 2004, the Texas Commission approved a rule delaying retail competition in our Texas service territory. This rule identified various milestones that we must reach before retail competition can begin. The first milestone calls for the development, approval by the Federal Energy Regulatory Commission (“FERC”), and commencement of independent operation of a regional transmission organization in the area that includes our service territory. This and other milestones are not likely to be achieved for a number of years. There is substantial uncertainty about both the regulatory framework and market conditions that would exist if and when retail competition is implemented in our Texas service territory, and we may incur substantial preparatory, restructuring and other costs that may not ultimately be recoverable. There can be no assurance that deregulation would not adversely affect our future operations, cash flows and financial condition.

We May Not Be Able to Recover All Our Planned Capital Expenditures

Our planned capital expenditures are large relative to our revenues and assets, and our ability to recover those capital expenditures and the timing of which recovery will have a significant impact on our results of operations. Any unexpected cost increases, delays or events that negatively impact our ability to raise capital, such as ratings downgrades or disruptions in the capital markets, or unexpected decisions or delays by the Texas Commission, NMPRC, or FERC in decisions affecting recovery of capital expenditures, could materially impact our financial statements.

Risks Related to the Offering

Increased leverage may harm our financial condition and results of operations.

We may incur additional indebtedness in the future and the Senior Notes do not restrict future incurrence of indebtedness. Any increase in our level of indebtedness will have several important effects on our future operations, including, without limitation:

- we will have additional cash requirements in order to support the payment of interest on our outstanding indebtedness;
- increases in our outstanding indebtedness and leverage will increase our vulnerability to adverse changes in general economic and industry conditions, as well as to competitive pressure; and
- depending on the levels of our outstanding debt, our ability to obtain additional financing for working capital, capital expenditures, general corporate and other purposes may be limited.

Our ability to make payments of principal and interest on our indebtedness depends upon our future performance, which will be subject to general economic conditions, industry cycles and financial, business and other factors affecting our operations, many of which are beyond our control. If we are unable to generate sufficient cash flow from operations in the future to service our debt, we may be required, among other things:

additional financing in the debt or equity markets;

restructure all or a portion of our indebtedness, including the Senior Notes;

assets;

reduce or delay planned capital expenditures; or

planned operating and investment expenditures.

- to seek

- to refinance or

- to sell selected

- to

- to reduce or delay

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These measures may not be sufficient to enable us to service our debt. In addition, any such financing, refinancing or sale of assets might not be available on economically favorable terms.

Ratings of the Senior Notes may change and affect the market price and marketability of the Senior Notes.

Our long term debt has been rated by Moody's Investors Service, Inc. and Standard & Poor's Ratings Services respectively. Such ratings are limited in scope, and do not address all material risks relating to an investment in the Senior Notes, but rather reflect only the view of each rating agency at the time the rating is issued. Our credit ratings may not remain in effect for any given period of time or such ratings will not be lowered, suspended or withdrawn entirely by the rating agencies, if, in each rating agency's judgment, circumstances so warrant. Our ratings may be lowered in connection with future events. Holders of Senior Notes will have no recourse against us or any other parties in the event of a change in or suspension or withdrawal of such ratings. Any lowering, suspension or withdrawal of such ratings may have an adverse effect on the market price or marketability of the Senior Notes.

The Senior Notes are effectively subordinated to any secured obligations we may have and to the obligations of our subsidiary.

Although the Senior Notes are unsubordinated obligations, they are effectively subordinated to any secured obligations we may have or may incur in the future, to the extent of the assets that serve as security for those obligations. As of the date of this prospectus supplement, we do not currently have any material secured obligations other than that portion of our obligations under our \$200,000,000 bank line of credit related to our financing of nuclear fuel purchases, which portion is secured by substantially all of our nuclear fuel assets. In addition, since the Senior Notes are exclusively our obligations and are not guaranteed by our subsidiary, the Senior Notes are also effectively subordinated to all liabilities of our subsidiary, to the extent of its assets, since it is a separate and distinct legal entity with no obligation to pay any amounts due under our indebtedness, including the Senior Notes, or to make any funds available to us, whether by paying dividends or otherwise, so that we can do so. Our subsidiary is not prohibited from incurring additional debt or other liabilities, including senior indebtedness, or from issuing equity interests that have priority over our interests in the subsidiary. If our subsidiary were to incur additional debt or liabilities or to issue equity interests that have priority over our interests in the subsidiary, our ability to pay our obligations on the Senior Notes could be adversely affected.

An active trading market for the Senior Notes may not develop.

There is currently no public market for the Senior Notes, and we do not plan to list the Senior Notes on any national securities exchange. In addition, the liquidity of any trading market in the Senior Notes, and the market price quoted for the Senior Notes, may be adversely affected by changes in the overall market for these Senior Notes, prevailing interest rates and changes in our financial condition, results of operations or prospects. A liquid trading market in the Senior Notes may not develop, which could decrease the amounts you would otherwise receive upon a sale or disposition of the Senior Notes.

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Use of Proceeds

The net proceeds from the sale of the Senior Notes will be approximately \$ million after the deduction of the underwriting discount and our expenses. We intend to use the net proceeds from the sale of the Senior Notes for general corporate purposes, which may include funding capital expenditures, repayment of debt and ensuring adequate liquidity.

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Capitalization

The following table sets forth our cash and cash equivalents and consolidated capitalization as of March 31, 2008 on an actual basis and on an as adjusted basis to give effect to the issuance of the Senior Notes offered by this prospectus supplement. This table should be read in conjunction with the financial statements and notes thereto incorporated by reference in this prospectus supplement and the accompanying prospectus.

| of March 31, 2008 | Actual | As Adjusted | (In Thousands) | Cash and Equivalents | \$ 11,725 | \$ | As Current |
|---|--------------|-------------|----------------|----------------------|-----------|----|---------------------------|
| Portion of Long-Term Debt and Financing Obligations | | | | 19,225 | | | 13,000 |
| Long-Term Debt Net of Current Portion | | 590,901 | | | | | 76,372 |
| % Senior Notes offered hereby | | — | | Total Debt | 699,498 | | Total Common Stock Equity |
| Total Capitalization | \$ 1,365,214 | \$ | | | | | 665,716 |

Under the terms of our credit facility, we have the ability to borrow up to \$200 million. As of March 31, 2008, we had \$108.6 million of indebtedness outstanding under our credit facility, \$13.0 million of which was drawn for working capital purposes.

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Description of the Senior Notes

The following description of the particular terms of the Senior Notes supplements, and to the extent inconsistent, replaces, the description in the accompanying prospectus of the general terms and provisions of the debt securities under “Description of Debt Securities” to which description reference is hereby made. Capitalized terms defined in the accompanying prospectus and not defined herein are used herein as therein defined.

General

The following is a summary of the terms of the Senior Notes. The Senior Notes will be issued under an indenture dated as of May 1, 2005 between us and The Bank of New York Trust Company, N.A., as successor to JPMorgan Chase Bank, National Association, as trustee (the “Trustee”), a copy of which is incorporated by reference as Exhibit 4.1 to the Registration Statement on Form S-3 of which the accompanying prospectus is a part, as amended by the First Supplemental Indenture dated as of May 19, 2008 between us and the Trustee in substantially the form attached as Exhibit 4.4 to such Registration Statement. The indenture, as amended by the supplemental indenture and as may be further supplemented from time to time, is referred to herein as the “Indenture.” This description is not complete and investors should refer to the Indenture. The Senior Notes will be established under the Indenture pursuant to a securities resolution.

Maturity, Interest, Form and Denomination

The Senior Notes will initially be issued in an amount equal to \$ _____ in aggregate principal amount. The Senior Notes will mature on _____, _____, unless redeemed prior to that date, and will bear interest at the rate of _____ % per year.

Interest on the Senior Notes will accrue from the date of original issuance and will be payable semi-annually in arrears on March 15 and September 15 of each year commencing on September 15, 2008 to holders of record of the Senior Notes on the preceding March 1 and September 1, respectively. If an interest payment date falls on a day that is not a business day, interest will be payable on the next succeeding business day with the same force and effect as if made on such interest payment date. Interest on the Senior Notes will be calculated on the basis of a 360-day year of twelve 30-day months. The notes will be issued in fully registered form in denominations of \$2,000 and in integral multiples of \$1,000 thereafter.

Further Issues of the Same Series

We may, from time to time, without the consent of the existing holders of the Senior Notes, issue additional debt securities under the Indenture having the same terms and CUSIP number as the Senior Notes in all respects, except for the issue date and the issue price. Any such additional debt securities will be consolidated with and form a single series with the Senior Notes offered hereby.

In addition to the Senior Notes, we may issue other series of debt securities under the Indenture. There is no limit on the total aggregate principal amount of debt securities that we can issue under the Indenture.

Optional Redemption

The Senior Notes will be redeemable in whole or in part, at our option, at any time and from time to time, at a redemption price equal to the greater of:

- (1) 100% of the principal amount of the Senior Notes to be redeemed or
- (2) the sum of the present values of the remaining scheduled payments of principal and interest thereon (exclusive of interest accrued to the redemption date) discounted to the redemption date on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at the Treasury Rate as defined below, plus basis points,
- plus, in either case, accrued and unpaid interest thereon to the redemption date.

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“Treasury Rate” means, with respect to any redemption date, the rate per annum equal to the semiannual equivalent yield to a maturity of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount equal to the Comparable Treasury Price for such redemption date). The Treasury Rate will be calculated on the third business day preceding the redemption date.

“Comparable Treasury Issue” means the United States Treasury security selected by an Independent Investment Banker as having a maturity comparable to the remaining term of the Senior Notes to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of such Senior Notes.

“Comparable Treasury Price” means, with respect to any redemption date, (1) the average of the Reference Treasury Dealer Quotations for such redemption date, after excluding the highest and lowest such Reference Treasury Dealer Quotations, or (2) if we obtain fewer than four such Reference Treasury Dealer Quotations, the average of all such Quotations.

“Independent Investment Banker” means one of the Reference Treasury Dealers that we appoint.

“Reference Treasury Dealers” means (1) Credit Suisse Securities (USA) LLC and its respective successors; provided, however, that if any of the foregoing shall cease to be a primary U.S. Government securities dealer (a “Primary Treasury Dealer”), we shall substitute another nationally recognized investment banking firm that is a Primary Treasury Dealer, and (2) two other Primary Treasury Dealers selected by us.

“Reference Treasury Dealer Quotations” means, with respect to each Reference Treasury Dealer and any redemption date, the average, as determined by us, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to us by such Reference Treasury Dealer at 5:00 p.m. on the third business day preceding such redemption date.

Notice of any redemption will be mailed at least 30 days but not more than 60 days before the redemption date to each holder of Senior Notes to be redeemed. Any notice of redemption at our option with respect to the Senior Notes may state that such redemption will be conditional upon the occurrence of any event before the redemption date described in such notice, and such notice will be of no force and effect unless all such conditions to the redemption have occurred on or before such redemption date. In the event that such conditions are not met, we will not be required to redeem the Senior Notes.

Unless we default in payment of the redemption price, on and after the redemption date, interest will cease to accrue on the Senior Notes or portions thereof called for redemption.

Limitation on Liens

So long as any Senior Notes are outstanding, we may not create or permit to be created, any mortgage, security interest, pledge, lien or other encumbrance (“Lien”) of or upon any of our Operating Property (as defined below), whether owned at the date of the Indenture or thereafter acquired, to secure any Debt (as defined below), without effectively securing the Senior Notes (together with, if we shall so determine, any of our other Debt ranking senior to, or equally with, the Senior Notes) equally and ratably with such Debt (but only so long as such Debt is so secured), subject to the following exceptions, one or more of which may apply to any particular Lien.

The foregoing restriction will not apply to:

secure Debt incurred without limitation as to amount under the Mortgage;

- Liens to
- Liens to secure

Debt existing on the date of the issuance of the Senior Notes; provided that such Debt shall not be increased in amount, except pursuant to our Credit Agreement dated as of April 11, 2006 as amended as of July 12, 2007 among the Company, The Bank of New York Trust Company, National Association, as trustee of the Rio Grande Resources Trust II, the lenders party thereto and JPMorgan Chase Bank, National Association as Administrative Agent and Issuing Bank;

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- Liens on any Operating Property which existed on such property prior to the acquisition thereof by us, to secure Debt assumed by us in connection with such acquisition;
- Liens to secure Debt incurred by the Company in connection with the acquisition or lease by the Company in the ordinary course of business, after the date of the issuance of the Senior Notes, of furniture, fixtures, equipment and other assets not owned by the Company as of the date of issuance of the Senior Notes provided that (a) such Debt shall not be secured by any Operating Property of the Company other than the Operating Property with respect to which such Debt is incurred, and (b) the Lien securing such Debt shall be created within 90 days of the incurrence of such Debt;
- Liens to secure Debt of any entity existing at the time such entity is merged into or consolidated with, or such entity disposes of all or substantially all its properties (or those of a division) to, us;
- Liens to secure Debt incurred to acquire, construct, develop or substantially repair, alter or improve Operating Property or to provide funds for any such purpose or for reimbursement of funds previously expended for any such purpose; provided that such Debt is incurred contemporaneously with, or within 24 months after, such acquisition or the completion of construction, development or substantial repair, alteration or improvement;
- Liens to secure, directly or indirectly, our obligations with respect to debt issued by any Governmental Authority (as defined herein), including debt represented by securities issued by any such Governmental Authority (or providers of credit enhancement with respect to such securities), including, without limitation, our obligations with respect to industrial development, pollution control or similar revenue bonds incurred for the purpose of financing all or any part of the purchase price or the cost of substantially repairing or altering, constructing, developing or substantially improving our Operating Property;
- Liens to secure Debt which has been defeased, including the Senior Notes;
- Liens to secure Debt incurred in connection with an accounts receivable facility and/or contract payments facility or the securitization of any Excepted Assets (as defined below); and
- Liens to secure any extension, renewal or replacement (or successive extensions, renewals or replacements), in whole or in part, of an instrument or agreement creating any Debt referred to in the above clauses.

Also, the foregoing restriction will not apply to Liens, otherwise subject to the foregoing restrictions, to secure Debt of up to an aggregate principal amount (not including Debt secured by Liens permitted by any of the foregoing exceptions) which, immediately following the creation of such Lien, together with all other Debt so secured, does not exceed 15% of Capitalization (as defined below). As of March 31, 2008, our Capitalization, as defined for purposes of this covenant, was approximately \$1,352 million.

For purposes of the limitation on liens covenant described above, certain terms are defined as follows:

“Capitalization” means the total of all the following items appearing on, or included in, our consolidated balance sheet:

- liabilities for Debt; and
- common stock, preferred stock, hybrid preferred securities, premium on capital stock, capital surplus, capital in excess of par value and retained earnings (however the foregoing may be designated), less, to the extent not otherwise deducted, the cost of shares of

our capital stock held in our treasury.

Subject to the foregoing, Capitalization shall be determined in accordance with generally accepted accounting principles applicable to the type of business in which we are engaged and that are

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approved by independent accountants regularly retained by us, and may be determined as of a date not more than sixty (60) days prior to the happening of an event for which such determination is being made.

“Debt” means any of our outstanding debt for money borrowed evidenced by notes, debentures, bonds, or other securities, or guarantees of any thereof.

“Excepted Assets” means all bills, notes and other instruments, accounts receivable, claims, credits, judgments, demands, general intangibles, licenses and privileges (except franchises and permits), emissions allowances, choses in action, patents, patent applications, patent licenses and other patent rights, trade names, trademarks and all contracts, leases and agreements of whatsoever kind and nature, other than any of the foregoing which are by the express provisions of the Mortgage subjected or required to be subjected to the Lien of the Mortgage.

“Governmental Authority” means any federal, state, local or foreign court or governmental agency, authority, instrumentality or regulatory body.

“Mortgage” means the General Mortgage Indenture and Deed of Trust dated February 1, 1996 between the Company and U.S. Bank National Association, successor to State Street Bank and Trust Company, as Trustee, as amended, supplemented, substituted or replaced from time to time; provided, however, that any such substitution or replacement will provide for a Lien on substantially all of the Company’s Operating Property subject to exceptions substantially similar to those contained in the previously existing Mortgage.

“Operating Property” means, as of any particular time, (i) all of the real, personal and mixed property which is an integral part of or is used or to be used as an integral part of the electric generating, transmission and/or distribution operations of the Company, (ii) any undivided legal interest of the Company in any such property which is jointly owned by the Company and any other person or persons and (iii) franchises and permits owned by the Company in connection with the electric generating, transmission and/or distribution operations of the Company, including, without limitation all of such property which is acquired by the Company after the date hereof; provided, however, that Operating Property shall not be deemed to include Excepted Property (as defined in the Mortgage). See “Description of First Mortgage Bonds — Mortgaged Property” in the accompanying prospectus.

Events of Default

The Senior Notes will be subject to the events of default contained in the indenture as described under “Description of Debt Securities — Defaults and Remedies” in the accompanying prospectus. In addition, pursuant to the securities resolution