FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

(Mark One)

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from _____ to _____

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

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

PINNACLE WEST CAPITAL CORPORATION	Yes ☑ No o
ARIZONA PUBLIC SERVICE COMPANY	Yes ☑ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

PINNACLE WEST CAPITAL CORPORATION	Yes o No o
ARIZONA PUBLIC SERVICE COMPANY	Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

PINNACLE WEST CAPITAL CORPORATION			
Large accelerated filer ☑	Accelerated filer o	Non-accelerated filer o	Smaller reporting company o
ARIZONA PUBLIC SERVICE COMPANY			
Large accelerated filer o	Accelerated filer o	Non-accelerated filer ☑	Smaller reporting company o

Indicate by check mark whether each registrant is a shell company (as defined in Exchange Act Rule 12b-2).

PINNACLE WEST CAPITAL CORPORATION	Yes o No ☑
ARIZONA PUBLIC SERVICE COMPANY	Yes o No ☑

Indicate the number of shares outstanding of each of the issuer’s classes of common stock as of the latest practicable date.

PINNACLE WEST CAPITAL CORPORATION	Number of shares of common stock, no par value, outstanding as of May 3, 2010: 108,447,282
ARIZONA PUBLIC SERVICE COMPANY	Number of shares of common stock, $2.50 par value, outstanding as of May 3, 2010: 71,264,947

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

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This combined Form 10-Q is separately provided by Pinnacle West Capital Corporation ("Pinnacle West") and Arizona Public Service Company ("APS"). Any use of the words "Company," "we," and "our" refer to Pinnacle West. Each registrant is providing on its own behalf all of the information contained in this Form 10-Q that relates to such registrant and, where required, its subsidiaries. Except as stated in the preceding sentence, neither registrant is providing any information that does not relate to such registrant, and therefore makes no representation as to any such information. The information required with respect to each company is set forth within the applicable items. Item 1 of this report includes Condensed Consolidated Financial Statements of Pinnacle West and Condensed Consolidated Financial Statements of APS. Item 1 also includes Notes to Pinnacle West's Condensed Consolidated Financial Statements, the majority of which also relates to APS, and Supplemental Notes, which only relate to APS' Condensed Consolidated Financial Statements. Item 2 of this report is divided into two sections — Pinnacle West Consolidated and APS. The Pinnacle West Consolidated section describes Pinnacle West and its subsidiaries on a consolidated basis, including discussions of Pinnacle West's regulated utility and non-utility operations.

FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements based on current expectations, and neither Pinnacle West nor APS assumes any obligation to update these statements, even if our internal estimates change, except as required by applicable law. These forward-looking statements are often identified by words such as “estimate,” “predict,” “may,” “believe,” “plan,” “expect,” “require,” “intend,” “assume” and similar words. Because actual results may differ materially from expectations, we caution readers not to place undue reliance on these statements. A number of factors could cause future results to differ materially from historical results, or from outcomes currently expected or sought by Pinnacle West or APS. In addition to the Risk Factors described in Item 1A of the Pinnacle West/APS Annual Report on Form 10-K for the fiscal year ended December 31, 2009 (“2009 Form 10-K”) and in Item 2 — Management’s Discussion and Analysis of Financial Condition and Results of Operation herein, these factors include, but are not limited to:

- regulatory and judicial decisions, developments and proceedings;
- our ability to achieve timely and adequate rate recovery of our costs;
- our ability to reduce capital expenditures and other costs while maintaining reliability and customer service levels;
- variations in demand for electricity, including those due to weather, the general economy, customer and sales growth (or decline), and the effects of energy conservation measures;
- power plant performance and outages;
- volatile fuel and purchased power costs;
- fuel and water supply availability;
- new legislation or regulation relating to greenhouse gas emissions, renewable energy mandates and energy efficiency standards;
- our ability to meet renewable energy requirements and recover related costs;
- risks inherent in the operation of nuclear facilities, including spent fuel disposal uncertainty;
- competition in retail and wholesale power markets;
- the duration and severity of the economic decline in Arizona and current credit, financial and real estate market conditions;
- the cost of debt and equity capital and the ability to access capital markets when required;
- restrictions on dividends or other burdensome provisions in our credit agreements and Arizona Corporation Commission (“ACC”) orders;
- our ability, or the ability of our subsidiaries, to meet debt service obligations;
- changes to our credit ratings;
- the investment performance of the assets of our nuclear decommissioning trust, pension, and other postretirement benefit plans and the resulting impact on future funding requirements;
- liquidity of wholesale power markets and the use of derivative contracts in our business;
- potential shortfalls in insurance coverage;
- new accounting requirements or new interpretations of existing requirements;
- transmission and distribution system conditions and operating costs;
- the ability to meet the anticipated future need for additional baseload generation and associated transmission facilities in our region;
- the ability of our counterparties and power plant participants to meet contractual or other obligations;
- technological developments in the electric industry; and
- economic and other conditions affecting the real estate market in SunCor Development Company’s (“SunCor”) market areas.

These and other factors are discussed in Risk Factors described in Item 1A of our 2009 Form 10-K, which readers should review carefully before placing any reliance on our financial statements or disclosures.

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

	Three Months Ended March 31,	
	2010	2009
OPERATING REVENUES		
Regulated electricity segment	$ 611,425	$ 602,578
Real estate segment	9,416	14,840
Other revenues	12,750	8,449
Total	633,591	625,867
OPERATING EXPENSES		
Regulated electricity segment fuel and purchased power	215,540	247,388
Real estate segment operations	13,890	26,910
Real estate impairment charge (Note 20)	15,112	208,480
Operations and maintenance	209,991	197,616
Depreciation and amortization	101,536	101,812
Taxes other than income taxes	31,827	34,128
Other expenses	8,061	6,467
Total	595,957	822,801
OPERATING INCOME (LOSS)	37,634	(196,934)
OTHER		
Allowance for equity funds used during construction	5,389	4,992
Other income (Note 14)	2,395	537
Other expense (Note 14)	(2,696)	(9,741)
Total	5,088	(4,212)
INTEREST EXPENSE		
Interest charges	62,054	59,035
Capitalized interest	(3,080)	(3,834)
Total	58,974	55,201
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	(16,252)	(256,347)
INCOME TAXES	(15,480)	(95,004)
LOSS FROM CONTINUING OPERATIONS	(772)	(161,343)
LOSS FROM DISCONTINUED OPERATIONS		
Net of income tax benefit of $81 and $3,063 (Note 17)	(125)	(4,727)
NET LOSS	(897)	(166,070)
Less: Net income (loss) attributable to noncontrolling interests (Notes 9 and 20)	5,117	(9,560)
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	$ (6,014)	$ (156,510)
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — BASIC	101,474	100,986
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — DILUTED	101,474	100,986
EARNINGS PER WEIGHTED-AVERAGE COMMON SHARE OUTSTANDING		
Loss from continuing operations attributable to common shareholders — basic	$ (0.06)	$ (1.50)
Net loss attributable to common shareholders — basic	$ (0.06)	$ (1.55)
Loss from continuing operations attributable to common shareholders — diluted	$ (0.06)	$ (1.50)
Net loss attributable to common shareholders — diluted	$ (0.06)	$ (1.55)
DIVIDENDS DECLARED PER SHARE	$ 0.525	$ 0.525
AMOUNTS ATTRIBUTABLE TO COMMON SHAREHOLDERS:		
Loss from continuing operations, net of tax	$ (5,889)	$ (151,783)
Discontinued operations, net of tax	(125)	(4,727)
Net loss attributable to common shareholders	$ (6,014)	$ (156,510)

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

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

	March 31, 2010	December 31, 2009
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 3,528	$ 145,378
Customer and other receivables	215,062	301,915
Accrued unbilled revenues	86,466	110,971
Allowance for doubtful accounts	(5,892)	(6,153)
Materials and supplies (at average cost)	171,118	176,020
Fossil fuel (at average cost)	37,907	39,245
Deferred income taxes	77,915	53,990
Income tax receivable (Note 8)	19,503	26,005
Assets from risk management activities (Note 10)	75,421	50,619
Other current assets	39,583	30,747
Total current assets	720,611	928,737
INVESTMENTS AND OTHER ASSETS		
Real estate investments — net (Note 20)	104,177	119,989
Assets from risk management activities (Note 10)	40,763	28,855
Nuclear decommissioning trust (Note 18)	433,399	414,576
Other assets	112,571	110,091
Total investments and other assets	690,910	673,511
PROPERTY, PLANT AND EQUIPMENT		
Plant in service and held for future use	12,849,716	12,848,138
Less accumulated depreciation and amortization	(4,349,437)	(4,340,645)
Net	8,500,279	8,507,493
Construction work in progress	528,940	467,700
Palo Verde sale leaseback, net of accumulated depreciation (Note 9)	144,528	146,722
Intangible assets, net of accumulated amortization	169,912	164,380
Nuclear fuel, net of accumulated amortization	142,254	118,243
Total property, plant and equipment	9,485,913	9,404,538
DEFERRED DEBITS		
Regulatory assets	863,233	813,161
Income tax receivable (Note 8)	65,103	65,103
Other	109,149	101,274
Total deferred debits	1,037,485	979,538
TOTAL ASSETS	$ 11,934,919	$ 11,986,324

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

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

	March 31, 2010	December 31, 2009
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 219,888	$ 240,637
Accrued taxes	127,513	104,011
Accrued interest	53,336	54,596
Short-term borrowings	289,616	153,715
Current maturities of long-term debt (Note 4)	489,626	303,476
Customer deposits	70,484	71,026
Liabilities from risk management activities (Note 10)	52,469	55,908
Other current liabilities	90,794	125,574
Total current liabilities	1,393,726	1,108,943
LONG-TERM DEBT LESS CURRENT MATURITIES		
Long-term debt (Note 4)	3,180,476	3,370,524
Palo Verde sale leaseback lessor notes (Notes 4 and 9)	126,000	126,000
Total long-term debt less current maturities	3,306,476	3,496,524
DEFERRED CREDITS AND OTHER		
Deferred income taxes	1,582,660	1,496,095
Deferred fuel and purchased power regulatory liability (Note 5)	105,378	87,291
Other regulatory liabilities	670,023	679,072
Liability for asset retirements	306,868	301,783
Liabilities for pension and other postretirement benefits (Note 6)	723,959	811,338
Liabilities from risk management activities (Note 10)	79,194	62,443
Customer advances	134,030	136,595
Coal mine reclamation	92,303	92,060
Unrecognized tax benefits (Note 8)	76,632	142,099
Other	133,670	144,077
Total deferred credits and other	3,904,717	3,952,853
COMMITMENTS AND CONTINGENCIES (SEE NOTES)		
EQUITY (Note 11)		
Common stock, no par value	2,155,977	2,153,295
Treasury stock	(2,734)	(3,812)
Total common stock	2,153,243	2,149,483
Retained earnings	1,238,940	1,298,213
Accumulated other comprehensive loss:		
Pension and other postretirement benefits	(50,048)	(50,892)
Derivative instruments	(128,202)	(80,695)
Total accumulated other comprehensive loss	(178,250)	(131,587)
Total Pinnacle West shareholders' equity	3,213,933	3,316,109
Noncontrolling interests (Note 9)	116,067	111,895
Total equity	3,330,000	3,428,004
TOTAL LIABILITIES AND EQUITY	$ 11,934,919	$ 11,986,324

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

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

	Three Months Ended March 31,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (897)	$ (166,070)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization including nuclear fuel	114,122	112,000
Deferred fuel and purchased power	44,040	28,238
Deferred fuel and purchased power amortization	(25,953)	28,961
Allowance for equity funds used during construction	(5,389)	(4,992)
Real estate impairment charge	15,112	215,869
Deferred income taxes	50,845	(3,901)
Change in mark-to-market valuations	1,842	3,822
Changes in current assets and liabilities:		
Customer and other receivables	60,244	76,390
Accrued unbilled revenues	24,505	15,365
Materials, supplies and fossil fuel	6,240	(11,796)
Other current assets	(8,836)	(711)
Accounts payable	(23,334)	(78,090)
Accrued taxes and income tax receivable-net	30,004	(81,846)
Other current liabilities	(36,582)	(29,658)
Expenditures for real estate investments	(443)	(1,459)
Gains and other changes in real estate assets	4,095	(264)
Change in margin and collateral accounts — assets	(11,280)	(23,476)
Change in margin and collateral accounts — liabilities	(124,495)	(162,013)
Change in unrecognized tax benefits	(62,062)	(1,050)
Change in other long-term assets	(25,903)	8,897
Change in other long-term liabilities	(39,550)	19,618
Net cash flow used for operating activities	(13,675)	(56,166)
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(202,554)	(193,014)
Contributions in aid of construction	2,949	18,762
Capitalized interest	(3,080)	(3,834)
Proceeds from nuclear decommissioning trust sales	158,448	129,816
Investment in nuclear decommissioning trust	(164,552)	(135,264)
Other	(1,639)	1,501
Net cash flow used for investing activities	(210,428)	(182,033)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	—	499,683
Repayment and reacquisition of long-term debt	(4,150)	(16,386)
Short-term borrowings and payments — net	135,901	(263,464)
Dividends paid on common stock	(51,421)	(51,196)
Common stock equity issuance	844	815
Other	1,079	(3,694)
Net cash flow provided by financing activities	82,253	165,758
NET DECREASE IN CASH AND CASH EQUIVALENTS	(141,850)	(72,441)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	145,378	105,245
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 3,528	$ 32,804
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Income taxes, net of (refunds)	$ (5,547)	$ 17,602
Interest, net of amounts capitalized	$ 58,679	$ 46,040

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

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Consolidation and Nature of Operations

The unaudited condensed consolidated financial statements include the accounts of Pinnacle West and our subsidiaries: APS, SunCor, APS Energy Services Company, Inc. ("APSES"), and El Dorado Investment Company ("El Dorado"). Intercompany accounts and transactions between the consolidated companies have been eliminated. The unaudited condensed consolidated financial statements for APS include the accounts of APS and the Palo Verde sale leaseback variable interest entities (see Note 9 for further discussion). Our accounting records are maintained in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Condensed Consolidated Financial Statements

Our condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments except as otherwise disclosed in the notes) that we believe are necessary for the fair presentation of our financial position, results of operations and cash flows for the periods presented. These condensed consolidated financial statements and notes have been prepared consistently with the exception of the reclassification of certain prior year amounts on our Condensed Consolidated Statements of Income, Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Cash Flows in accordance with accounting requirements for reporting discontinued operations (see Note 17) and amended accounting guidance on consolidation of variable interest entities (see Note 9).

3. Quarterly Fluctuations

Weather conditions cause significant seasonal fluctuations in our revenues. In addition, real estate activities, such as the real estate impairment charges recorded in 2009 and 2010 (see Note 20), can have significant impacts on our results for interim periods. For these reasons, results for interim periods do not necessarily represent results expected for the year.

4. Long-term Debt and Liquidity Matters

The following table shows principal payments due on Pinnacle West's and APS' total long-term debt and capitalized lease requirements as of March 31, 2010 (dollars in millions):

Year	Consolidated Pinnacle West	APS
2010	$ 315	$ 223
2011	632	457
2012	478	478
2013	59	59
2014	503	503
Thereafter	1,816	1,816
Total	$ 3,803	$ 3,536

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Credit Facilities and Debt Issuances

Pinnacle West and APS maintain credit facilities in order to enhance liquidity and provide credit support. During the first quarter of 2010, Pinnacle West and APS refinanced existing revolving credit facilities that would have matured in December 2010. In addition, Pinnacle West and APS accessed the commercial paper market, which neither company had utilized since the third quarter of 2008 due to negative market conditions.

Pinnacle West

On February 12, 2010, Pinnacle West refinanced its $283 million revolving credit facility that would have matured in December 2010, and decreased the size of the facility to $200 million. The new facility matures February 2013. Pinnacle West has the option to increase the amount of the facility up to a maximum of $300 million upon the satisfaction of certain conditions and with the consent of the lenders. Pinnacle West will use the facility for general corporate purposes, repayment of long-term debt, commercial paper support and for the issuance of letters of credit. Interest rates are based on Pinnacle West's senior unsecured debt credit ratings. As a result of the downsized revolving credit facility, the Company also reduced the size of its commercial paper program to $200 million from $250 million.

At March 31, 2010, the $200 million revolver was available to support the issuance of up to $200 million in commercial paper or to be used as bank borrowings, including issuances of letters of credit up to $100 million. At March 31, 2010 the Company had outstanding $10 million of borrowings under its revolving credit facility and no letters of credit. In addition, Pinnacle West had commercial paper borrowings of $80 million at March 31, 2010.

In April 2010, Pinnacle West issued 6,900,000 shares of common stock at an offering price of $38.00 per share, resulting in net proceeds of approximately $253 million. Pinnacle West contributed all of the proceeds from this offering to APS. APS anticipates using these capital contributions to repay short-term indebtedness, to finance capital expenditures and for other general corporate purposes.

APS

On February 12, 2010, APS refinanced its $377 million revolving credit facility that would have matured in December 2010, and increased the size of the facility to $500 million. The new revolving credit facility terminates in February 2013. APS has the option to increase the amount of the facility up to a maximum of $700 million upon the satisfaction of certain conditions and with the consent of the lenders. APS will use the facility for general corporate purposes, commercial paper support and for the issuance of letters of credit. Interest rates are based on APS' senior unsecured debt credit ratings.

At March 31, 2010 APS had two committed revolving credit facilities totaling $989 million, including the $500 million credit facility described above and a $489 million facility that terminates in September 2011. The revolvers are available either to support the issuance of up to $250 million in commercial paper or to be used for bank borrowings, including issuances of letters of credit up to $739 million. At March 31, 2010, APS had borrowings of $70 million under its $489 million credit facility and no letters of credit under its revolving credit facilities. APS had commercial paper borrowings of $125 million at March 31, 2010.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

On January 1, 2010, due to the adoption of amended accounting guidance relating to variable interest entities ("VIEs"), APS began consolidating the Palo Verde Lessor Trusts (see Note 9) and, as a result of consolidation of these VIEs, we have reported the Lessor Trusts' long-term debt on our Condensed Consolidated Balance Sheets. Interest rates on these debt instruments are 8% and are fixed for the remaining life. As of March 31, 2010, approximately $26 million was classified as current maturities of long-term debt and $126 million was classified as long-term debt relating to these VIEs. These debt instruments mature on December 30, 2015 and have sinking fund features that are serviced by the lease payments. See Note 9 for additional discussion of the VIEs.

SunCor

SunCor's principal loan facility (the "SunCor Secured Revolver") is secured primarily by an interest in land, commercial properties and land contracts. At March 31, 2010, SunCor had outstanding borrowings of approximately $54 million under the SunCor Secured Revolver, which matured on January 30, 2010. SunCor and the lenders under the SunCor Secured Revolver have signed a forbearance agreement under which the lenders have agreed not to exercise any remedies prior to June 30, 2010 to allow time for SunCor to continue discussions concerning the potential sale of additional properties. In addition to the SunCor Secured Revolver, at March 31, 2010, SunCor had approximately $42 million of outstanding debt under other credit facilities ($26 million of which has matured and remains outstanding). To date, the lenders under these credit facilities have taken no enforcement action. At March 31, 2010, $92 million was classified as current maturities of long-term debt and $4 million was classified as short-term borrowings on our Condensed Consolidated Balance Sheets.

If SunCor is unable to obtain extensions or renewals of the SunCor Secured Revolver or its other matured debt, or if it is unable to comply with the mandatory repayment and other provisions of any new or modified credit agreements, SunCor could be required to immediately repay its outstanding indebtedness under all of its credit facilities as a result of cross-default provisions. Such an immediate repayment obligation would have a material adverse impact on SunCor's business and financial position and impair its ongoing viability.

SunCor cannot predict the outcome of negotiations with its lenders or its ability to sell assets for sufficient proceeds to repay its outstanding debt (see Note 20). SunCor's ability to generate sufficient cash from operations while it pursues lender negotiations and further asset sales is uncertain.

Neither Pinnacle West nor any of its other subsidiaries has guaranteed any SunCor indebtedness. A SunCor debt default would not result in a cross-default of any of the debt of Pinnacle West or any of its other subsidiaries. While there can be no assurances as to the ultimate outcome of this matter, Pinnacle West does not believe that SunCor's inability to obtain extensions or renewals from SunCor's lenders would have a material adverse impact on Pinnacle West's cash flows or liquidity.

As of March 31, 2010, SunCor could not transfer any cash dividends to Pinnacle West as a result of the covenants mentioned above. The restriction does not affect Pinnacle West's ability to meet its ongoing capital requirements.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Debt Provisions

An existing ACC order requires APS to maintain a common equity ratio of at least 40%. As defined in the ACC order, the common equity ratio is common equity divided by the sum of common equity and long-term debt, including current maturities of long-term debt. At March 31, 2010, APS' common equity ratio, as defined, was 50%. Its total common equity was approximately $3.4 billion, and total capitalization was approximately $6.7 billion. APS would be prohibited from paying dividends if the payment would reduce its common equity below approximately $2.7 billion, assuming APS' total capitalization remains the same. This restriction does not materially affect Pinnacle West's ability to meet its ongoing capital requirements.

5. Regulatory Matters

2008 General Retail Rate Case Impacts

On December 30, 2009, the ACC issued an order approving a settlement agreement ("Settlement Agreement") entered into by APS and twenty-one other parties to its general retail rate case, which was originally filed in March 2008. The Settlement Agreement contains on-going requirements, commitments and authorizations, including the following:

- Revenue accounting treatment for line extension payments received for new or upgraded service from January 1, 2010 through year end 2012 (or until new rates are established in APS' next general rate case, if that is before the end of 2012), resulting in present estimates of increased revenues of $23 million, $25 million and $49 million, respectively;
- An authorized return on common equity of 11.0%;
- A capital structure comprised of 46.2% debt and 53.8% common equity;
- A commitment from APS to reduce average annual operational expenses by at least $30 million from 2010 through 2014;
- Authorization and requirements of equity infusions into APS of at least $700 million during the period beginning June 1, 2009 through December 31, 2014 ($253 million of which was infused into APS as of May 6, 2010 from proceeds of a Pinnacle West equity issuance (see Note 4)); and
- Various modifications to the existing energy efficiency, demand-side management and renewable energy programs that require APS to, among other things, expand its conservation and demand-side management programs and its use of renewable energy, as well as allow for concurrent recovery of renewable energy expenses and provide for more concurrent recovery of demand-side management costs and incentives.

The parties also agreed to a rate case filing plan in which APS is prohibited from filing its next two general rate cases until on or after June 1, 2011 and June 1, 2013, respectively, unless certain extraordinary events occur. Subject to the foregoing, APS may not request its next general retail rate increase to be effective prior to July 1, 2012. APS currently expects it will file its next rate case in June 2011. The parties agreed to use good faith efforts to process these subsequent rate cases within twelve months of sufficiency findings from the ACC staff, which generally occur within 30 days after the filing of a rate case.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Cost Recovery Mechanisms

APS has received supportive regulatory decisions that allow for more timely recovery of certain costs through the following recovery mechanisms.

Renewable Energy Standard. In 2006, the ACC approved the Arizona Renewable Energy Standard and Tariff ("RES"). Under the RES, electric utilities that are regulated by the ACC must supply an increasing percentage of their retail electric energy sales from eligible renewable resources, including solar, wind, biomass, biogas and geothermal technologies. In order to achieve these requirements, the ACC allows APS to include a RES surcharge on customer bills to recover the approved amounts for use on renewable energy projects. Each year APS is required to file a five-year implementation plan with the ACC and seek approval for the upcoming year's RES funding amount.

During 2009, APS filed its annual RES implementation plan, covering the 2010-2014 timeframe and requesting 2010 RES funding approval. The plan provides for the acquisition of renewable generation in compliance with requirements through 2014, and requests RES funding of $86.7 million for 2010. APS also sought various other determinations in its plan, including approval of the AZ Sun program and the Community Power Project in Flagstaff, Arizona. At its December 2009 open meeting, the ACC approved APS' 2010 RES funding request.

On March 3, 2010, the ACC approved the AZ Sun program, which contemplates the addition of 100 megawatts ("MW") of utility-owned solar resources through 2014. Through the expected life of the program, APS plans to invest up to $500 million for turn-key photovoltaic power plants across Arizona. Developers will be selected through competitive procurement processes to build the plants, which APS will own. The costs associated with the first 50 MW under this program will be recovered initially through the RES until such time as the costs are recovered in base rates. The costs of the second 50 MW will be recovered through a mechanism to be determined in APS's next retail rate case.

On April 1, 2010 the ACC approved the Community Power Project, a pilot program in which APS will own, operate and receive energy from solar panels on the rooftops of up to 200 residential and business customers located within a certain test area. Third party developers may also own systems that participate in the pilot. Costs of the program will be recovered through the RES until such time as the costs are recovered in base rates.

Demand-Side Management Adjustor Charge ("DSMAC"). The Settlement Agreement requires APS to submit an annual Energy Efficiency Implementation Plan for review by and approval of the ACC. On July 15, 2009, APS filed its initial Energy Efficiency Implementation Plan, requesting approval by the ACC of programs and program elements for which APS has estimated a budget in the amount of $49.9 million for 2010. In order to recover these estimated amounts for use on certain demand-side management programs, a surcharge would be added to customer bills similar to that described above under the RES. The surcharge will offset energy efficiency expenses and allow for the recovery of any earned incentives. APS received ACC approval of all of its proposed programs and implemented the new DSMAC on March 1, 2010.

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The ACC approved recovery of the 2010 Energy Efficiency budget less some $1.0 million, which reflected a recalculation of the incentive payment due to APS under the Energy Efficiency Implementation Plan and not a reduction in allowed program costs. The ACC also approved recovery of all 2009 program costs plus incentives. The change from program cost recovery on a historical basis to recovery on a concurrent basis, as authorized in the Settlement Agreement, resulted in this one-time need to address two years (2009 and 2010) of cost recovery. As requested by APS, 2009 program cost recovery is to be spread over a three-year period.

PSA Mechanism and Balance. The power supply adjustor ("PSA") provides for the adjustment of retail rates to reflect variations in retail fuel and purchased power costs. The following table shows the changes in the deferred fuel and purchased power regulatory asset (liability) for the three-month periods ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Beginning balance	$ (87)	$ 8
Deferred fuel and purchased power costs-current period	(44)	(28)
Amounts refunded (recovered)	26	(29)
Ending balance	$ (105)	$ (49)

The PSA rate for the current PSA Year is ($0.0045) per kilowatt hour ("kWh"). Since the 2010 PSA adjustment was a reduction of the PSA rate, the ACC accelerated the 2010 adjustment from the standard PSA year start date of February 1st to January 1st to coincide with the increase in retail rates resulting from the ACC's decision in the general retail rate case, causing a minimal net impact on residential bills. This accelerated 2010 adjustment will remain in effect until February 1, 2011. The $105 million regulatory liability at March 31, 2010 reflects lower average prices and the seasonal nature of fuel and purchased power costs. Any uncollected (overcollected) deferrals during the 2010 PSA Year will be included in the historical component of the PSA rate for the PSA Year beginning February 1, 2011.

The PSA rate for the PSA Year that began February 1, 2009 was $0.0053 per kWh. The PSA rate may not be increased or decreased more than $0.004 per kWh in a year without permission of the ACC.

Transmission Rates and Transmission Cost Adjustor. In July 2008, the United States Federal Energy Regulatory Commission ("FERC") approved an Open Access Transmission Tariff for APS to move from fixed rates to a formula rate-setting methodology in order to more accurately reflect the costs that APS incurs in providing transmission services. A large portion of the rate represents charges for transmission services to serve APS' retail customers ("Retail Transmission Charges"). In order to recover the Retail Transmission Charges, APS must file an application with, and obtain approval from, the ACC under the transmission cost adjustor ("TCA") mechanism, by which changes in Retail Transmission Charges can be reflected in APS' retail rates.

The formula rate is updated, or "trued-up", each year effective June 1 on the basis of APS' actual cost of service, as disclosed in APS' FERC Form 1 report for the previous fiscal year. Items to be updated include actual capital expenditures made as compared with previous projections, transmission revenue credits and other items. The resolution of proposed adjustments can result in significant volatility in the revenues to be collected. APS reviews the proposed formula rate filing amounts with the ACC staff. Any items or adjustments which are not agreed to by APS and the ACC staff can remain in dispute until settled or litigated at FERC. Settlement or litigated resolution of disputed issues could require an extended period of time and have a significant effect on the Retail Transmission Charge because any adjustment, though applied prospectively, may be calculated to account for previously over-collected amounts.

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In 2009, APS was authorized to implement an increase in its annual transmission revenues based on calculations filed with the FERC using data for its 2008 fiscal year. Increases in APS' annual transmission revenues of $22.8 million became effective June 1, 2009. Of this amount, $21 million represents an increase in Retail Transmission Charges, which was approved by the ACC on July 29, 2009 and allows APS to reflect the related increased Retail Transmission Charges in its retail rates through the TCA effective August 1, 2009. The 2010 TCA will be filed with the ACC in mid-May.

6. Retirement Plans and Other Benefits

Pinnacle West sponsors a qualified defined benefit and account balance pension plan, a non-qualified supplemental excess benefit retirement plan, and other postretirement benefit plans for the employees of Pinnacle West and our subsidiaries. Pinnacle West uses a December 31 measurement date for its pension and other postretirement benefit plans. The market-related value of our plan assets is their fair value at the measurement date.

On March 23, 2010, the President signed into law comprehensive health care reform legislation under the Patient Protection and Affordable Care Act (the "Act"). One feature of the Act is the elimination of the tax deduction for prescription drug costs that are reimbursed as part of the Medicare Part D subsidy. Although this tax increase does not take effect until 2013, we are required to recognize the full accounting impact in our financial statements in the period in which the Act is signed. In accordance with accounting for regulated companies, the loss of this deduction is substantially offset by a regulatory asset that will be recovered through future electric revenues. In the first quarter of 2010, Pinnacle West charged regulatory assets and liabilities for a total of $42 million, with a corresponding increase in accumulated deferred income tax liabilities, to reflect the impact of this change in tax law.

The following table provides details of the plans' net periodic benefit costs and the portion of these costs charged to expense (including administrative costs and excluding amounts capitalized as overhead construction or billed to electric plant participants) (dollars in millions):

	Pension Benefits		Other Benefits	
	Three Months Ended March 31,		Three Months Ended March 31,	
	2010	2009	2010	2009
Service cost — benefits earned during the period	$ 15	$ 14	$ 5	$ 5
Interest cost on benefit obligation	31	29	11	10
Expected return on plan assets	(31)	(29)	(10)	(9)
Amortization of:				
Transition obligation	—	—	1	1
Prior service cost	1	1	—	—
Net actuarial loss	6	3	3	3
Net periodic benefit cost	$ 22	$ 18	$ 10	$ 10
Portion of cost charged to expense	$ 11	$ 8	$ 5	$ 5
APS' share of cost charged to expense	$ 10	$ 8	$ 5	$ 5

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Contributions

The required minimum contribution to our pension plan is zero in 2010. During the first quarter of 2010 we made a voluntary contribution of $100 million to our pension plan. The contribution to our other postretirement benefit plans in 2010 is estimated to be approximately $15 million. APS and other subsidiaries fund their share of the contributions. APS' share is approximately 97% of both plans.

7. Business Segments

Pinnacle West's two reportable business segments are:

- our regulated electricity segment, which consists of traditional regulated retail and wholesale electricity businesses (primarily retail and wholesale sales supplied to traditional cost-based rate regulation ("Native Load") customers) and related activities and includes electricity generation, transmission and distribution; and
- our real estate segment, which consists of SunCor's real estate development and investment activities

Financial data for the three months ended March 31, 2010 and 2009 and at March 31, 2010 and December 31, 2009 is provided as follows (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Operating revenues:		
Regulated electricity segment	$ 611	$ 603
Real estate segment (a)	10	15
All other (b)	13	8
Total	$ 634	$ 626
Net income (loss) attributable to common shareholders:		
Regulated electricity segment	$ 7	$ (20)
Real estate segment (a)	(13)	(132)
All other (b)	—	(5)
Total	$ (6)	$ (157)

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	As of March 31, 2010	As of December 31, 2009
Assets:		
Regulated electricity segment	$ 11,686	$ 11,691
Real estate segment (a)	133	161
All other (b)	116	134
Total	$ 11,935	$ 11,986

(a) In 2009 our real estate subsidiary, SunCor, began disposing of substantially all of its assets (see Note 20). As a result, the real estate segment may no longer be a reporting segment in the future.

(b) Includes activities related to APSES and El Dorado. None of the activities of either of these companies constitutes a reportable segment.

8. Income Taxes

Pinnacle West expects to recognize approximately $131 million of cash tax benefits related to SunCor's strategic asset sales (see Note 20), which will not be fully realized until all the asset sale transactions are completed. Approximately $6 million of these benefits were recorded in the three months ended March 31, 2010 as reductions to income tax expense related to the current impairment charges. The additional $125 million of tax benefits were recorded as reductions to income tax expense related to SunCor impairment charges recorded on or before December 31, 2009.

The $85 million income tax receivable on the Condensed Consolidated Balance Sheets represents the anticipated refunds related to an APS tax accounting method change approved by the Internal Revenue Service ("IRS") in the third quarter of 2009 and the current year tax benefits related to the SunCor strategic asset sales that closed prior to March 31, 2010.

During the first quarter of 2010, the Company reached a settlement with the IRS with regard to the examination of tax returns for the years ended December 31, 2005 through 2007. As a result of this settlement, net uncertain tax positions have decreased by $62 million through March 31, 2010, including approximately $3.5 million which decreased our effective tax rate. Additionally, the settlement resulted in the recognition of net interest benefits of approximately $3 million through the effective tax rate.

As of March 31, 2010, the tax year ended December 31, 2008 and all subsequent tax years remain subject to examination by the IRS. With few exceptions, we are no longer subject to state income tax examinations by tax authorities for years before 1999.

9. Variable Interest Entities

On January 1, 2010 we adopted amended accounting guidance relating to VIEs. This amended guidance significantly changed the consolidation model for VIEs. Under the prior guidance the consolidation model considered risk absorption using a quantitative approach when determining the primary beneficiary. The consolidation model under the new guidance requires a qualitative assessment and focuses on the powers to direct activities of the VIE when determining the primary beneficiary. As a result of applying this qualitative assessment we have determined that APS is the primary beneficiary of certain VIEs, and is therefore required to consolidate these VIEs. Prior to adopting this new guidance APS was not considered the primary beneficiary of these VIEs and did not consolidate these entities. We have adopted this guidance using retrospective application and have adjusted prior periods presented to reflect consolidation of the VIEs in those periods. Further discussion follows regarding the impact of the consolidation.

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APS VIEs

In 1986, APS entered into agreements with three separate VIE lessor trusts in order to sell and lease back interests in Palo Verde Nuclear Generating Station ("Palo Verde") Unit 2 and related common facilities. The VIE lessor trusts are single-asset leasing entities. APS will pay approximately $49 million per year for the years 2010 to 2015 related to these leases. The leases do not contain fixed price purchase options or residual value guarantees. However, the lease agreements include fixed-rate renewal periods which may have a significant impact on the VIEs' economic performance. We have concluded that these fixed rate renewal periods may give APS the ability to utilize the asset for a significant portion of the asset's economic life, and therefore provide APS with the power to direct activities of the VIEs that most significantly impact the VIEs' economic performance. In addition to the fixed rate renewal periods, our primary beneficiary analysis also considered that we are the operating agent for Palo Verde, are obligated to decommission the leased assets and have fair value purchase options.

Under the previous quantitative VIE consolidation model, APS was not considered the primary beneficiary of the lessor trusts as APS did not absorb the majority of the entities' expected losses or did not receive a majority of the residual returns. The arrangements were previously accounted for as operating leases.

Consolidation of these VIEs eliminates the lease accounting we previously reported and results in changes in our consolidated assets, debt, equity, and net income. Assets of the VIEs are restricted and may only be used to settle the VIEs' debt and for payment to the noncontrolling interest holders. The creditors of the VIEs have no recourse to the general credit of APS or Pinnacle West. As a result of consolidation we have eliminated rent expense, and have recognized depreciation and interest expense, resulting in an increase in net income of $5 million entirely attributable to the noncontrolling interests. Income attributable to Pinnacle West shareholders remains the same. Consolidation of these VIEs also results in changes to our Condensed Consolidated Statements of Cash Flows, but does not impact net cash flows.

Our Condensed Consolidated Balance Sheets at March 31, 2010 include the following amounts relating to the VIEs (in millions):

	March 31, 2010
Property plant and equipment, net of accumulated depreciation	$ 145
Long-term debt including current maturities	152
Equity- Noncontrolling interests	87

For regulatory ratemaking purposes the leases continue to be treated as operating leases, and as a result we have recorded a regulatory asset of $32 million as of March 31, 2010.

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APS is exposed to losses relating to these lessor trust VIEs upon the occurrence of certain events that APS does not consider to be reasonably likely to occur. Under certain circumstances (for example, the NRC issuing specified violation orders with respect to Palo Verde or the occurrence of specified nuclear events), APS would be required to make specified payments to the VIEs' noncontrolling equity participants, assume the VIEs' debt, and take title to the leased Unit 2 interests, which, if appropriate, may be required to be written down in value. If such an event had occurred as of March 31, 2010, APS would have been required to pay the noncontrolling equity participants approximately $153 million and assume $152 million of debt. Since APS now consolidates the VIEs, the debt APS would be required to assume is already reflected in our Condensed Consolidated Balance Sheets.

We also have certain long-term purchased power agreements to purchase substantially all of an entity's output from a specified facility for a specified period. We have evaluated these arrangements under the VIE accounting guidance and have determined that these agreements do not represent variable interests. If these agreements had been deemed variable interests in these entities, we would not be considered the primary beneficiary of these entities, as we do not have the power to direct activities of these entities in a manner that would significantly impact their economic performance and therefore would not consolidate the entities. The adoption of the amended accounting guidance has not changed how we account for these arrangements.

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Prior-Year Periods

We have elected to apply the amended guidance retrospectively for all prior periods presented on Pinnacle West's Condensed Consolidated Statements of Income, Balance Sheets, and Statements of Cash Flows. The following table presents the financial statement line item changes (dollars in thousands):

	As previously reported	Reclassifications as a result of the adoption of new VIE accounting guidance	Amount reported after adoption of amended VIE accounting guidance
Statement of Income for the three months ended March 31, 2009			
Operating Expenses — Operations and maintenance	$ 207,531	$ (9,915)	$ 197,616
Operating Expenses — Depreciation and amortization	99,886	1,926	101,812
Interest Expense — Interest Charges	55,696	3,339	59,035
Loss from Continuing Operations	(165,993)	4,650	(161,343)
Net Loss	(170,720)	4,650	(166,070)
Net income (loss) attributable to noncontrolling interests	(14,210)	4,650	(9,560)
Balance Sheets — December 31, 2009			
Property, Plant and Equipment — Palo Verde sale leaseback, net of accumulated depreciation	$ —	$ 146,722	$ 146,722
Deferred Debits — Regulatory assets	781,714	31,447	813,161
Current Liabilities — Current maturities of long-term debt	277,693	25,783	303,476
Long-Term Debt Less Current Maturities — Palo Verde sale leaseback lessor notes	—	126,000	126,000
Deferred Credits and Other — Other	200,015	(55,938)	144,077
Equity — Noncontrolling Interests	29,571	82,324	111,895
Statement of Cash Flows for the three months ended March 31, 2009			
Cash Flows from Operating Activities — Net loss	$ (170,720)	$ 4,650	$ (166,070)
Cash Flows from Operating Activities — Depreciation and amortization including nuclear fuel	110,073	1,927	112,000
Cash Flows from Operating Activities — Change in other current liabilities	(20,744)	(8,914)	(29,658)
Cash Flows from Operating Activities — Change in other long-term liabilities	17,281	2,337	19,618

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SunCor VIEs

SunCor is the primary beneficiary of certain land development trust arrangements and, accordingly, consolidates these VIEs. We have determined that SunCor is the primary beneficiary of these VIEs because SunCor controls the activities related to the development of the land held in the trusts. Our adoption of amended VIE accounting guidance has not changed our accounting treatment of the SunCor VIEs. Our Condensed Consolidated Balance Sheets reflect $29 million of assets and $29 million of noncontrolling equity interests relating to these arrangements at March 31, 2010 and December 31, 2009. The assets relating to these VIEs consist strictly of land, all of which is restricted and may only be used for payment to the noncontrolling interests. We have not provided, and are not required to provide, financing or other financial support to these entities.

10. Derivative and Energy Trading Accounting

We are exposed to the impact of market fluctuations in the commodity price and transportation costs of electricity, natural gas, coal, emissions allowances and in interest rates. We manage risks associated with these market fluctuations by utilizing various derivative instruments, including futures, forwards, options and swaps. As part of our overall risk management program, we may use such instruments to hedge purchases and sales of electricity, fuels, and emissions allowances and credits. Derivative instruments that are designated as cash flow hedges are used to limit our exposure to cash flow variability on forecasted transactions. The changes in market value of such contracts have a high correlation to price changes in the hedged transactions.

Our derivative instruments are accounted for at fair value and are presented on the Condensed Consolidated Balance Sheets as “Assets/Liabilities from Risk Management Activities” (see Note 19 for a discussion of fair value measurements). Derivative instruments for the physical delivery of purchase and sale quantities transacted in the normal course of business qualify for the normal purchase and sales scope exception and are accounted for under the accrual method of accounting. Due to the scope exception, these derivative instruments are excluded from our derivative instrument discussion and disclosures below.

We enter into derivative instruments for economic hedging purposes. While we believe the economic hedges mitigate exposure to fluctuations in commodity prices, some of these instruments may not meet the specific hedge accounting requirements and are not designated as accounting hedges. Economic hedges not designated as accounting hedges are recorded at fair value on our balance sheet with changes in fair value recognized in the statement of income as incurred. These instruments are included in the “non-designated hedges” discussion and disclosure below.

Hedge effectiveness is the degree to which the derivative instrument contract and the hedged item are correlated and is measured based on the relative changes in fair value between the derivative instrument contract and the hedged item over time. We assess hedge effectiveness both at inception and on a continuing basis. These assessments exclude the time value of certain options. For accounting hedges that are deemed an effective hedge, the effective portion of the gain or loss on the derivative instrument is reported as a component of accumulated other comprehensive income (“AOCI”) and reclassified into earnings in the same period during which the hedged transaction affects earnings. We recognize in current earnings the gains and losses representing hedge ineffectiveness, and the gains and losses on any hedge components which are excluded from our effectiveness assessment. As of March 31, 2010, we hedged the majority of certain exposures to the price variability of commodities for a maximum of 39 months.

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In the electricity business, some contracts to purchase energy are netted against other contracts to sell energy. This is called "book-out" and usually occurs in contracts that have the same terms (quantities and delivery points) and for which power does not flow. We net these book-outs, which reduces both revenues and fuel and purchased power costs in our Condensed Consolidated Statements of Income, but this does not impact our financial condition, net income or cash flows.

For its regulated operations, APS defers for future rate treatment approximately 90% of unrealized gains and losses on certain derivatives pursuant to the PSA mechanism that would otherwise be recognized in income. Realized gains and losses on derivatives are deferred in accordance with the PSA to the extent the amounts are above or below the portion of APS' retail base rates attributable to fuel and purchased power costs ("Base Fuel Rate"), which is currently $0.0376 per kWh (see Note 5). Gains and losses from derivatives in the following tables represent the amounts reflected in income before the effect of PSA deferrals.

As of March 31, 2010, we had the following outstanding gross notional amount of derivatives, which represent both purchases and sales (does not reflect net position):

Commodity	Quantity	
Power	15,928,321	megawatt hours
Gas	157,264,840	MMBTU (a)

(a) "MMBTU" is one million British thermal units

Derivative Instruments in Designated Accounting Hedging Relationships

The following table provides information about gains and losses from derivative instruments in designated accounting hedging relationships and their impact on our Condensed Consolidated Statements of Income during the three months ended March 31, 2010 and 2009 (dollars in thousands):

Commodity Contracts	Financial Statement Location	Three Months Ended March 31, 2010	2009
Amount of Loss Recognized in AOCI on Derivative Instruments (Effective Portion)	Accumulated other comprehensive loss-derivative instruments	$ (91,667)	$ (138,548)
Amount of Loss Reclassified from AOCI into Income (Effective Portion Realized)	Regulated electricity segment fuel and purchased power	(13,185)	(25,365)
Amount of Gain (Loss) Recognized in Income from Derivative Instruments (Ineffective Portion and Amount Excluded from Effectiveness Testing) (a)	Regulated electricity segment fuel and purchased power	(10,467)	992

(a) During the three months ended March 31, 2010 and 2009, we had no amounts reclassified from AOCI to earnings related to discontinued cash flow hedges.

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During the next twelve months, we estimate that a net loss of $118 million before income taxes will be reclassified from AOCI as an offset to the effect of market price changes for the related hedged transactions. Approximately 90% of the amounts related to derivatives subject to the PSA will be recorded as either a regulatory asset or liability and have no effect on earnings.

Derivative Instruments Not Designated as Accounting Hedges

The following table provides information about gains and losses from derivative instruments not designated as accounting hedging instruments and their impact on our Condensed Consolidated Statements of Income during the three months ended March 31, 2010 and 2009 (dollars in thousands):

Commodity Contracts	Financial Statement Location	Three Months Ended March 31, 2010	2009
Amount of Net Gain (Loss) Recognized in Income from Derivative Instruments	Regulated electricity segment revenue	$ 170	$ (429)
Amount of Net Loss Recognized in Income from Derivative Instruments	Regulated electricity segment fuel and purchased power expense	(34,969)	(63,964)
Total		$ (34,799)	$ (64,393)

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Fair Values of Derivative Instruments in the Condensed Consolidated Balance Sheets

The following table provides information about the fair value of our derivative instruments, margin account and cash collateral reported on a gross basis. Transactions with counterparties that have master netting arrangements are reported net on the balance sheet. These amounts are located in the assets and liabilities from risk management activities lines of our Condensed Consolidated Balance Sheets. Amounts are as of March 31, 2010 (dollars in thousands):

Commodity Contracts	Current Assets	Investments and Other Assets	Current Liabilities	Deferred Credits and Other	Total Assets (Liabilities)
Derivatives designated as accounting hedging instruments:					
Assets	$ —	$ —	$ —	$ 18	$ 18
Liabilities	(1,381)	—	(132,258)	(112,704)	(246,343)
Total hedging instruments	(1,381)	—	(132,258)	(112,686)	(246,325)
Derivatives not designated as accounting hedging instruments:					
Assets	41,278	40,780	59,403	47,986	189,447
Liabilities	(2,384)	(17)	(117,972)	(103,669)	(224,042)
Total non-hedging instruments	38,894	40,763	(58,569)	(55,683)	(34,595)
Total derivatives	37,513	40,763	(190,827)	(168,369)	(280,920)
Margin account	20,402	—	9,336	258	29,996
Collateral provided to counterparties	23,256	—	130,072	88,917	242,245
Collateral provided from counterparties	(5,750)	—	(1,050)	—	(6,800)
Balance Sheet Total	$ 75,421	$ 40,763	$ (52,469)	$ (79,194)	$ (15,479)

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The following table provides information about the fair value of our derivative instruments, margin account and cash collateral reported on a gross basis at December 31, 2009 (dollars in thousands):

Commodity Contracts	Current Assets	Investments and Other Assets	Current Liabilities	Deferred Credits and Other	Total Assets (Liabilities)
Derivatives designated as accounting hedging instruments:					
Assets	$ 329	$ —	$ 3,242	$ 75	$ 3,646
Liabilities	(3,436)	(256)	(72,899)	(77,953)	(154,544)
Total hedging instruments	(3,107)	(256)	(69,657)	(77,878)	(150,898)
Derivatives not designated as accounting hedging instruments:					
Assets	31,220	29,807	34,645	44,631	140,303
Liabilities	(4,123)	(696)	(81,722)	(71,408)	(157,949)
Total non-hedging instruments	27,097	29,111	(47,077)	(26,777)	(17,646)
Total derivatives	23,990	28,855	(116,734)	(104,655)	(168,544)
Margin account	8,643	—	12,464	104	21,211
Collateral provided to counterparties	17,986	—	49,412	42,108	109,506
Collateral provided from counterparties	—	—	(1,050)	—	(1,050)
Balance Sheet Total	$ 50,619	$ 28,855	$ (55,908)	$ (62,443)	$ (38,877)

Credit Risk and Credit Related Contingent Features

We are exposed to losses in the event of nonperformance or nonpayment by counterparties. We have risk management contracts with many counterparties, including one counterparty for which our exposure represents approximately 31% of Pinnacle West's $116 million of risk management assets as of March 31, 2010. This exposure relates to a long-term traditional wholesale contract with a counterparty that has very high credit quality. Our risk management process assesses and monitors the financial exposure of all counterparties. Despite the fact that the great majority of trading counterparties' debt is rated as investment grade by the credit rating agencies, there is still a possibility that one or more of these companies could default, resulting in a material impact on consolidated earnings for a given period. Counterparties in the portfolio consist principally of financial institutions, major energy companies, municipalities and local distribution companies. We maintain credit policies that we believe minimize overall credit risk to within acceptable limits. Determination of the credit quality of our counterparties is based upon a number of factors, including credit ratings and our evaluation of their financial condition. To manage credit risk, we employ collateral requirements and standardized agreements that allow for the netting of positive and negative exposures associated with a single counterparty. Valuation adjustments are established representing our estimated credit losses on our overall exposure to counterparties.

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Certain of our derivative instrument contracts contain credit-risk-related contingent features including, among other things, investment grade credit rating provisions, credit-related cross default provisions, and adequate assurance provisions. Adequate assurance provisions allow a counterparty with reasonable grounds for uncertainty to demand additional collateral based on subjective events and/or conditions. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that were in a liability position on March 31, 2010 was $425 million, for which we had posted collateral of $222 million in the normal course of business.

For those derivative instruments in a net liability position, with investment grade credit contingencies, the counterparties could demand additional collateral if our debt credit rating were to fall below investment grade (below BBB- for Standard & Poor's Ratings Services ("Standard & Poor's") or Fitch, Inc. ("Fitch") or Baa3 for Moody's Investors Service, Inc. ("Moody's")), which would be a violation of the credit rating provisions. If the investment grade contingent features underlying these agreements had been triggered on March 31, 2010, after off-setting asset positions under master netting arrangements we would have been required to post approximately an additional $80 million of collateral to our counterparties; this amount includes those contracts which qualify for scope exceptions, which are excluded from the derivative details in the above footnote. We also have energy related non-derivative instrument contracts with investment grade credit-related contingent features which could also require us to post additional collateral of approximately $200 million if our debt credit ratings were to fall below investment grade.

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11. Changes in Equity

The following tables show Pinnacle West's changes in shareholders' equity and changes in equity of noncontrolling interests for the three months ended March 31, 2010 and 2009 (dollars in thousands):

	Three Months Ended March 31, 2010			Three Months Ended March 31, 2009		
	Shareholders' Equity	Noncontrolling Interests	Total	Shareholders' Equity	Noncontrolling Interests	Total
Beginning balance, January 1	$ 3,316,109	$ 111,895	$3,428,004	$ 3,445,979	$ 124,990	$3,570,969
Net income (loss)	(6,014)	5,117	(897)	(156,510)	(9,560)	(166,070)
Other comprehensive loss:						
Net unrealized losses on derivative instruments (a)	(91,667)	—	(91,667)	(138,548)	—	(138,548)
Net reclassification of realized losses to income (b)	13,185	—	13,185	25,365	—	25,365
Reclassification of pension and other postretirement benefits to income	1,393	—	1,393	1,252	—	1,252
Income tax benefit related to items of other comprehensive income	30,426	—	30,426	44,003	—	44,003
Total other comprehensive loss	(46,663)	—	(46,663)	(67,928)	—	(67,928)
Total comprehensive income (loss)	(52,677)	5,117	(47,560)	(224,438)	(9,560)	(233,998)
Issuance of capital stock	2,680	—	2,680	2,629	—	2,629
Purchase of treasury stock, net of reissuances	1,078	—	1,078	(1,551)	—	(1,551)
Other	2	(22)	(20)	(6,707)	(129)	(6,836)
Common stock dividends	(53,259)	—	(53,259)	(53,010)	—	(53,010)
Net capital activities by noncontrolling interests	—	(923)	(923)	—	1,316	1,316
Ending balance, March 31	$ 3,213,933	$ 116,067	$3,330,000	$ 3,162,902	$ 116,617	$3,279,519

(a) These amounts primarily include unrealized gains and losses on contracts used to hedge our forecasted electricity and natural gas requirements to serve Native Load. These changes are primarily due to changes in forward natural gas prices and wholesale electricity prices.

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

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12. Commitments and Contingencies

Palo Verde Nuclear Generating Station

Spent Nuclear Fuel and Waste Disposal

Nuclear power plant operators are required to enter into spent fuel disposal contracts with the United States Department of Energy ("DOE"), and the DOE is required to accept and dispose of all spent nuclear fuel and other high-level radioactive wastes generated by domestic power reactors. Although the Nuclear Waste Policy Act required the DOE to develop a permanent repository for the storage and disposal of spent nuclear fuel by 1998, the DOE announced that it would not be able to open the repository by 1998 and sought to excuse its performance under the contract. In November 1997, the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit) issued a decision preventing the DOE from excusing its own delay, but refused to order the DOE to begin accepting spent nuclear fuel.

Based on this decision and the DOE's delay, a number of utilities, including APS (on behalf of itself and the other Palo Verde owners), filed damages actions against the DOE in the Court of Federal Claims. APS is currently pursuing that damages claim. The trial in the APS matter began on January 28, 2009, and closing arguments were heard in late May 2009. The court has not indicated when it will reach its decision in the matter. In January 2010, on appeal of another utility's damages case in which the DOE successfully raised the unavoidable delays defense, the Court of Appeals for the Federal Circuit reversed the lower court's decision and concluded that the Court of Federal Claims, the court handling the APS matter, is bound by the November 1997 D.C. Circuit decision that prevents the DOE from excusing its delay in performance.

APS currently estimates it will incur $132 million (in 2010 dollars) over the current life of Palo Verde for its share of the costs related to the on-site interim storage of spent nuclear fuel. At March 31, 2010, APS had a regulatory liability of $37 million that represents amounts recovered in retail rates in excess of amounts spent for on-site interim spent fuel storage.

Fuel and Purchased Power Commitments

APS is party to various fuel and purchased power contracts with terms expiring between 2010 and 2042 that include required purchase provisions. APS estimates the contract requirements to be approximately $469 million in 2010; $341 million in 2011; $360 million in 2012; $466 million in 2013; $498 million in 2014; and $6.7 billion thereafter. However, these amounts may vary significantly pursuant to certain provisions in such contracts that permit us to decrease required purchases under certain circumstances. These amounts have increased since the 2009 Form 10-K due to increased solar contracts to meet our increasing requirements.

Renewable Energy Credits

In 2010, APS entered into additional contracts to purchase renewable energy credits to comply with the RES. APS estimates the new level of contract requirements at March 31, 2010 to be approximately $33 million in 2010; $19 million in 2011; $19 million in 2012; $19 million in 2013; $19 million in 2014; and $209 million thereafter.

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California Energy Market Issues and Refunds in the Pacific Northwest

In July 2001, the FERC ordered an expedited fact-finding hearing to calculate refunds for spot market transactions in California during a specified time frame. APS was a seller and a purchaser in the California markets at issue and, to the extent that refunds are ordered, APS should be a recipient as well as a payor of such amounts. In addition, on March 19, 2002, the State of California filed a complaint with the FERC alleging that wholesale sellers of power and energy, including APS, failed to properly file rate information at the FERC in connection with sales to California from 2000 to March 2002 under market-based rates. Since 2004, the Ninth Circuit and the FERC have issued various decisions and orders involving the aforementioned issues, including decisions related to: entities subject to FERC jurisdiction and, therefore, potentially owing refunds; applicable refund methodologies; the temporal scope and types of transactions that are properly subject to the refund orders; and the appropriate standard of review at the FERC on wholesale power contracts in the refund proceedings. A settlement, resolving APS' issues with certain California parties for the current refund period, was approved by the FERC in an order issued on June 30, 2008. The resolution of the claims related to the parties involved in this settlement had no material adverse impact on our financial position, results of operations or cash flows. We currently believe the refund claims at the FERC related to the parties not involved in this settlement will have no material adverse impact on our financial position, results of operations or cash flows.

On July 25, 2001, the FERC also ordered an evidentiary proceeding to discuss and evaluate possible refunds for wholesale sales in the Pacific Northwest. The FERC affirmed the administrative law judge's conclusion that the prices in the Pacific Northwest were not unreasonable or unjust and refunds should not be ordered in this proceeding. This decision was appealed to the U.S. Court of Appeals for the Ninth Circuit. On August 24, 2007, the Ninth Circuit issued an opinion that remanded the proceeding to the FERC for further consideration. Although the FERC has not yet determined whether any refunds will ultimately be required, we do not expect that the resolution of these issues will have a material adverse impact on our financial position, results of operations or cash flows.

Superfund

The Comprehensive Environmental Response, Compensation and Liability Act ("Superfund") establishes liability for the cleanup of hazardous substances found contaminating the soil, water or air. Those who generated, transported or disposed of hazardous substances at a contaminated site are among those who are potentially responsible parties under Superfund ("PRPs"). PRPs may be strictly, and often are jointly and severally, liable for clean-up. On September 3, 2003, the United States Environmental Protection Agency ("EPA") advised APS that the EPA considers APS to be a PRP in the Motorola 52nd Street Superfund Site, Operable Unit 3 (OU3) in Phoenix, Arizona. APS has facilities that are within this Superfund site. APS and Pinnacle West have agreed with the EPA to perform certain investigative activities of the APS facilities within OU3. In addition, on September 23, 2009, APS agreed with the EPA and one other PRP to voluntarily assist with the funding and management of the site-wide groundwater remedial investigation and feasibility study work plan. We estimate that our costs related to this investigation and study will be approximately $1.2 million, which is reserved as a liability on our financial statements. We anticipate incurring additional expenditures in the future, but because the overall investigation is not complete and ultimate remediation requirements are not yet finalized, at the present time we cannot accurately estimate our total expenditures.

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Landlord Bankruptcy

On April 16, 2009, the landlord for our corporate headquarters building announced that it is seeking relief under Chapter 11 of the United States Bankruptcy Code. At March 31, 2010, we have several assets on our books related to our landlord, the most significant of which is an asset related to levelized rent payments for the building of approximately $67 million which is included in other deferred debits on the Condensed Consolidated Balance Sheets. This amount will continue to increase to approximately $94 million as a result of the lease terms until 2015, when this amount will begin to decrease over the remaining life of the lease. We are monitoring this matter and, while there can be no assurances as to the ultimate outcome of the matter due to the complexity of the bankruptcy proceedings, we currently do not expect that it will have a material adverse effect on our financial position, results of operations, or cash flows.

13. Nuclear Insurance

The Palo Verde participants are insured against public liability for a nuclear incident up to $12.6 billion per occurrence. As required by the Price Anderson Nuclear Industries Indemnity Act, Palo Verde maintains the maximum available nuclear liability insurance in the amount of $375 million, which is provided by commercial insurance carriers. The remaining balance of $12.2 billion is provided through a mandatory industry wide retrospective assessment program. If losses at any nuclear power plant covered by the program exceed the accumulated funds, APS could be assessed retrospective premium adjustments. The maximum assessment per reactor under the program for each nuclear incident is approximately $118 million, subject to an annual limit of $18 million per incident, to be periodically adjusted for inflation. Based on APS' interest in the three Palo Verde units, APS' maximum potential assessment per incident for all three units is approximately $103 million, with an annual payment limitation of approximately $15 million.

The Palo Verde participants maintain "all risk" (including nuclear hazards) insurance for property damage to, and decontamination of, property at Palo Verde in the aggregate amount of $2.75 billion, a substantial portion of which must first be applied to stabilization and decontamination. APS has also secured insurance against portions of any increased cost of generation or purchased power and business interruption resulting from a sudden and unforeseen accidental outage of any of the three units. The property damage, decontamination, and replacement power coverages are provided by Nuclear Electric Insurance Limited ("NEIL"). APS is subject to retrospective assessments under all NEIL policies if NEIL's losses in any policy year exceed accumulated funds. The maximum amount APS could incur under the current NEIL policies totals approximately $16 million for each retrospective assessment declared by NEIL's Board of Directors due to losses. In addition, NEIL policies contain rating triggers that would result in APS providing approximately $44 million of collateral assurance within 20 business days of a rating downgrade to non-investment grade. The insurance coverage discussed in this and the previous paragraph is subject to certain policy conditions and exclusions.

PINNACLE WEST CAPITAL CORPORATION
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14. Other Income and Other Expense

The following table provides detail of other income and other expense for the three months ended March 31, 2010 and 2009 (dollars in thousands):

	Three Months Ended March 31,	
	2010	2009
Other income:		
Interest income	$ 875	$ 261
SunCor other income (a)	286	93
Investment gains — net	1,222	—
Miscellaneous	12	183
Total other income	$ 2,395	$ 537
Other expense:		
Non-operating costs	$ (1,794)	$ (1,608)
Investment losses — net	—	(7,230)
Miscellaneous	(902)	(903)
Total other expense	$ (2,696)	$ (9,741)

(a) Includes equity earnings from a real estate joint venture that is a pass-through entity for tax purposes.

15. Guarantees

We have issued parental guarantees and letters of credit and obtained surety bonds on behalf of our subsidiaries.

Our parental guarantees for APS relate to commodity energy products. In addition, Pinnacle West has obtained approximately $9 million of surety bonds related to APS' operations, which primarily relate to self-insured workers' compensation. Our credit support instruments enable APSES to offer energy-related products. Non-performance or non-payment under the original contract by our subsidiaries would require us to perform under the guarantee or surety bond. No liability is currently recorded on the Condensed Consolidated Balance Sheets related to Pinnacle West's current outstanding guarantees on behalf of our subsidiaries. At March 31, 2010, we had no guarantees that were in default. Our guarantees have no recourse or collateral provisions to allow us to recover amounts paid under the guarantees. The amounts and approximate terms of our guarantees and surety bonds for each subsidiary at March 31, 2010 are as follows (dollars in millions):

	Guarantees		Surety Bonds	
	Amount	Term (in years)	Amount	Term (in years)
APSES	$ 9	1	$ 28	1
APS	3	1	9	1
Total	$ 12		$ 37	

APS has entered into various agreements that require letters of credit for financial assurance purposes. At March 31, 2010, approximately $227 million of letters of credit were outstanding to support existing pollution control bonds of approximately $224 million. The letters of credit are available to fund the payment of principal and interest of such debt obligations and expire in 2010. APS has also entered into approximately $62 million of letters of credit to support certain equity lessors in the Palo Verde sale leaseback transactions (see Note 9 for further details on the Palo Verde sale leaseback transactions). These letters of credit were amended and extended in April 2010, and will expire in 2013.

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

16. Earnings Per Share

The following table presents earnings per weighted average common share outstanding for the three months ended March 31, 2010 and 2009:

	Three Months Ended March 31,	
	2010	2009
Basic earnings per share:		
Loss from continuing operations attributable to common shareholders	$ (0.06)	$ (1.50)
Loss from discontinued operations	—	(0.05)
Loss per share — basic	$ (0.06)	$ (1.55)
Diluted earnings per share:		
Loss from continuing operations attributable to common shareholders	$ (0.06)	$ (1.50)
Loss from discontinued operations	—	(0.05)
Loss per share — diluted	$ (0.06)	$ (1.55)

For the three months ended March 31, 2010 and 2009 the weighted average common shares outstanding were the same for both basic and diluted shares. Options to purchase 387,800 shares of common stock for the three-month period ended March 31, 2010 and 625,524 shares for the three-month period ended March 31, 2009 were outstanding but were excluded from the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

17. Discontinued Operations

SunCor (real estate segment) **—** In 2009, SunCor sold properties that are required to be reported as discontinued operations on Pinnacle West's Condensed Consolidated Statements of Income. Prior year income statement amounts related to these properties were reclassified from operations to discontinued operations. In addition, see Note 20 — Real Estate Impairment Charge.

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The following table contains SunCor's revenue, loss before income taxes and loss after taxes classified as discontinued operations in Pinnacle West's Condensed Consolidated Statements of Income for the three months ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Revenue	$ —	$ 4
Loss before income taxes	—	(8)
Loss after taxes (a)	—	(5)

(a) Includes a tax benefit recognized by the parent company in accordance with an intercompany tax sharing agreement of $3 million for the three months ended March 31, 2009.

18. Nuclear Decommissioning Trust

To fund the costs APS expects to incur to decommission Palo Verde, APS established external decommissioning trusts in accordance with Nuclear Regulatory Commission ("NRC") regulations. Third-party investment managers are authorized to buy and sell securities per their stated investment guidelines. The trust funds are invested in a tax efficient manner in fixed income securities and domestic equity securities. APS classifies investments in decommissioning trust funds as available for sale. As a result, we record the decommissioning trust funds at their fair value on our Condensed Consolidated Balance Sheets. Because of the ability of APS to recover decommissioning costs in rates and in accordance with the regulatory treatment for decommissioning trust funds, we have recorded the offsetting amount of gains or losses on investment securities in other regulatory liabilities or assets. The following table summarizes the fair value of APS' nuclear decommissioning trust fund assets at March 31, 2010 and December 31, 2009 (dollars in millions):

	Fair Value	Total Unrealized Gains	Total Unrealized Losses
March 31, 2010			
Equity securities	$ 150	$ 34	$ (3)
Fixed income securities	298	11	(1)
Net payables (a)	(15)	—	—
Total	$ 433	$ 45	$ (4)

(a) Net payables relate to pending securities sales and purchases.

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	Fair Value	Total Unrealized Gains	Total Unrealized Losses
December 31, 2009			
Equity securities	$ 167	$ 37	$ (6)
Fixed income securities	247	11	(1)
Net receivables (a)	1	—	—
Total	$ 415	$ 48	$ (7)

(a) Net receivables relate to pending securities sales and purchases.

The costs of securities sold are determined on the basis of specific identification. The following table sets forth approximate gains and losses and proceeds from the sale of securities by the nuclear decommissioning trust funds (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Realized gains	$ 12	$ 2
Realized losses	(2)	(2)
Proceeds from the sale of securities (a)	158	130

(a) Proceeds are reinvested in the trust.

The fair value of fixed income securities, summarized by contractual maturities, at March 31, 2010 is as follows (dollars in millions):

	Fair Value
Less than one year	$ 32
1 year – 5 years	79
5 years – 10 years	77
Greater than 10 years	110
Total	$ 298

See Note 19 for a discussion of fair value measurements.

19. Fair Value Measurements

We disclose the fair value of certain assets and liabilities according to a fair value hierarchy. This hierarchy ranks the quality and reliability of the inputs used to determine fair values, which are then classified and disclosed in one of three categories. The three levels of the fair value hierarchy are:

Level 1 — Quoted prices in active markets for identical assets or liabilities. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide information on an ongoing basis. This category includes derivative instruments that are exchange-traded such as futures, cash equivalents invested in exchange-traded money market funds, exchange-traded equities, and investments in Treasury securities.

Level 2 — Quoted prices in active markets for similar assets or liabilities; quoted prices in markets that are not active; and model-derived valuations whose inputs are observable. This category includes nonexchange-traded derivative such as forwards, options, and swaps. This category also includes investments in common and commingled funds that are redeemable and valued based on the funds' net asset values.

Level 3 — Model-derived valuations with unobservable inputs that are supported by little or no market activity. Instruments in this category include long-dated derivative transactions where models are required due to the length of the transaction, certain options, transactions in locations where observable market data does not exist, and common and collective trusts with significant restrictions on our ability to transact in the fund. The valuation models we employ utilize spot prices, forward prices, historical market data and other factors to forecast future prices. The primary valuation technique we use to calculate the fair value of contracts where price quotes are not available is based on the extrapolation of forward pricing curves using observable market data for more liquid delivery points in the same region and actual transactions at the more illiquid delivery points.

Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. We maximize the use of observable inputs and minimize the use of unobservable inputs. If market data is not readily available, inputs may reflect our own assumptions about the inputs market participants would use. Our assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels. Thus, a valuation may be classified in Level 3 even though the valuation may include significant inputs that are readily observable. We assess whether a market is active by obtaining observable broker quotes, reviewing actual market transactions, and assessing the volume of transactions. We consider broker quotes observable inputs when the quote is binding on the broker, we can validate the quote with market transactions, or we can determine that the inputs the broker used to arrive at the quoted price are observable.

Recurring Fair Value Measurements

We apply recurring fair value measurements to derivative instruments, nuclear decommissioning trusts, certain cash equivalents and plan assets held in our retirement and other benefit plans.

Some of our derivative instrument transactions are valued based on unobservable inputs due to the long-term nature of contracts or the unique location of the transactions. Our long-dated energy transactions consist of observable valuations for the near term portion and unobservable valuations for the long-term portions of the transaction. When the unobservable portion is significant to the overall valuation of the transaction, the entire transaction is classified as Level 3. Our classification of instruments as Level 3 is primarily reflective of the long-term nature of our energy transactions, and is not reflective of material inactive markets.

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The nuclear decommissioning trust invests in fixed income securities directly and equity securities indirectly through commingled funds. The commingled equity funds are valued based on the fund's net asset value ("NAV") and are classified within Level 2. We may transact in the fund on a semi-monthly basis. Our trustee provides valuation of our nuclear decommissioning trust assets by using pricing services to determine fair market value. We assess these valuations and verify that pricing can be supported by actual recent market transactions. The trust fund investments have been established to satisfy APS' nuclear decommissioning obligations (see Note 18).

For non-exchange traded contracts, we calculate fair market value based on the average of the bid and offer price, discounted to reflect net present value. We maintain certain valuation adjustments for a number of risks associated with the valuation of future commitments. These include valuation adjustments for liquidity and credit risks based on the financial condition of counterparties. The liquidity valuation adjustment represents the cost that would be incurred if all unmatched positions were closed-out or hedged.

The credit valuation adjustment represents estimated credit losses on our overall exposure to counterparties, taking into account netting arrangements, expected default experience for the credit rating of the counterparties and the overall diversification of the portfolio. Counterparties in the portfolio consist principally of major energy companies, municipalities, local distribution companies and financial institutions. We maintain credit policies that management believes minimize overall credit risk. Determination of the credit quality of counterparties is based upon a number of factors, including credit ratings, financial condition, project economics and collateral requirements. When applicable, we employ standardized agreements that allow for the netting of positive and negative exposures associated with a single counterparty.

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The following table presents the fair value at March 31, 2010 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in millions):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (a) (Level 3)	Counterparty Netting & Other (b)	Balance at March 31, 2010
Assets					
Risk management activities (c)	$ 2	$ 132	$ 55	$ (73)	$ 116
Nuclear decommissioning trust:					
U.S. Treasury debt securities	66	—	—	—	66
Commingled U.S. equity funds	—	150	—	—	150
Corporate debt securities	—	64	—	—	64
Mortgage-backed securities	—	63	—	—	63
Municipality debt securities	—	49	—	—	49
Other	—	56	—	(15)	41
Total	$ 68	$ 514	$ 55	$ (88)	$ 549
Liabilities					
Risk management activities (c)	$ (12)	$ (372)	$ (86)	$ 338	$ (132)

(a) Primarily consists of long-dated electricity contracts.

(b) Primarily represents netting under master netting arrangements, including margin and collateral. See Note 10.

(c) Commodity contracts. See Note 10.

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The following table presents the fair value at December 31, 2009 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in millions):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (a) (Level 3)	Counterparty Netting & Other (b)	Balance at December 31, 2009
Assets					
Cash equivalents	$ 97	$ —	$ —	$ —	$ 97
Risk management activities (c)	1	100	42	(64)	79
Nuclear decommissioning trust:					
U.S. Treasury debt securities	55	—	—	—	55
Commingled U.S. equity funds	—	167	—	—	167
Corporate debt securities	—	62	—	—	62
Mortgage-backed securities	—	60	—	—	60
Municipality debt securities	—	49	—	—	49
Other	—	21	—	1	22
Total	$ 153	$ 459	$ 42	$ (63)	$ 591
Liabilities					
Risk management activities (c)	$ (14)	$ (246)	$ (52)	$ 194	$ (118)

(a) Primarily consists of long-dated electricity contracts.

(b) Primarily represents netting under master netting arrangements, including margin and collateral. See Note 10.

(c) Commodity Contracts. See Note 10.

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The following table shows the changes in fair value for assets and liabilities that are measured at fair value on a recurring basis using Level 3 inputs for the three months ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Net derivative balance at beginning of period	$ (10)	$ (7)
Total net gains (losses) realized/unrealized:		
Included in earnings (a)	(1)	2
Included in other comprehensive income ("OCI")	(6)	(1)
Deferred as a regulatory asset	(12)	(3)
Transfers into Level 3 from Level 2 (b)	—	(14)
Transfers from Level 3 into Level 2 (b)	(2)	—
Net derivative balance at end of period	$ (31)	$ (23)
Net unrealized gains (losses) included in earnings related to instruments still held at end of period	$ (1)	$ 2

(a) Earnings are recorded in regulated electricity segment revenue or regulated electricity segment fuel and purchased power.

(b) We had no significant Level 1 transfers to or from any other hierarchy level. Transfers in or out of Level 3 reflect the fair market value at the beginning of the period. Transfers are triggered by a change in the lowest significant input during the period. Transfers are typically related to our long-dated energy transactions that extend beyond available quoted periods.

Nonrecurring Fair Value Measurements

We may be required to record other assets at fair value on a nonrecurring basis. These nonrecurring fair value measurements typically involve write-downs of individual assets due to impairment.

We apply nonrecurring fair value measurements to certain real estate assets. These adjustments to fair value are the result of write-downs of individual assets due to impairment. Certain of our real estate assets have been impaired due to the distressed real estate market. We determine fair value for our real estate assets primarily based on the future cash flows that we estimate will be generated by each asset discounted for market risk. These fair value determinations require significant judgment regarding key assumptions. Due to these unobservable inputs, the valuation of real estate assets are considered Level 3 measurements.

As of March 31, 2010, the fair value of our impaired real estate assets that are measured at fair value on a nonrecurring basis was $72 million, all of which was valued using significant unobservable inputs (Level 3). Total impairment charges included in net income for the three months ended March 31, 2010 were approximately $15 million. See Note 20 for additional information.

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Financial Instruments Not Carried at Fair Value

The following table represents the carrying amount and estimated fair value of our debt which is not carried at fair value on the balance sheet. The carrying value of our cash, net accounts receivable, accounts payable and short-term borrowings approximate fair value. Certain of our debt instruments contain third-party credit enhancements and, in accordance with GAAP, we do not consider the effect of these credit enhancements when determining fair value. Our debt fair value estimates are based on quoted market prices of the same or similar issues (dollars in millions):

	As of March 31, 2010		As of December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Pinnacle West	$ 175	$ 180	$ 175	$ 180
APS	3,529	3,727	3,530	3,667
SunCor	92	92	95	95
Total	$ 3,796	$ 3,999	$ 3,800	$ 3,942

20. Real Estate Impairment Charge

In 2009, SunCor undertook and completed a review of its assets and strategies within its various markets as a result of the distressed conditions in real estate and credit markets. Based on the results of the review, on March 27, 2009, SunCor's Board of Directors authorized a series of strategic transactions to dispose of SunCor's homebuilding operations, master-planned communities, land parcels, commercial assets and golf courses in order to reduce SunCor's outstanding debt. During 2009, we recorded impairment charges of approximately $266 million pre-tax and $161 million after income taxes. In the first quarter of 2010, we recorded impairment charges of approximately $15 million pre-tax and $9 million after income taxes related to held and used assets. We believe that the assets to be sold, which are classified as "Real Estate Investments — Net" on the Condensed Consolidated Balance Sheets, do not meet the held for sale and discontinued operations criteria as of March 31, 2010, because of the uncertainties related to the current market conditions and obtaining necessary approvals. The detail of the impairment charge is as follows (dollars in millions, and before income taxes):

	Three Months Ended March 31,	
	2010	2009
Homebuilding and master-planned communities	$ 1	$ 140
Land parcels and commercial assets	9	51
Golf courses	1	18
Other	4	—
Subtotal	15	209
Discontinued operations	—	7
Less noncontrolling interests	—	(14)
Total	$ 15	$ 202

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

We estimate the fair value of our real estate assets primarily based on either the future cash flows that we estimate will be generated by each asset discounted at a rate we believe market participants would use, on independent appraisals, or other market information, including comparison to comparable properties. Our impairment assessments and fair value determinations require significant judgment regarding key assumptions such as future sales prices, future construction and land development costs, future sales timing, and discount rates. The assumptions are specific to each project and may vary among projects. The weighted average discount rates we used to estimate fair values during 2009 and 2010 ranged from 11% to 29%. Due to the judgment and assumptions applied in the estimation process, with regard to impairments, it is possible that actual results could differ from those estimates.

SunCor also recorded $8 million of pretax severance and other charges relating to these actions during the three months ended March 31, 2009. Pinnacle West does not expect that any of the impairment charges will result in future cash expenditures, other than immaterial disposition costs.

See Note 4 for a discussion of SunCor’s debt and liquidity matters, and the impact of impairment charges on the SunCor Secured Revolver.

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

	Three Months Ended March 31,	
	2010	2009
ELECTRIC OPERATING REVENUES	$ 611,476	$ 602,660
OPERATING EXPENSES		
Fuel and purchased power	215,540	247,388
Operations and maintenance	203,881	191,185
Depreciation and amortization	100,609	99,937
Income taxes	(5,440)	(6,744)
Other taxes	31,451	33,780
Total	546,041	565,546
OPERATING INCOME	65,435	37,114
OTHER INCOME (DEDUCTIONS)		
Income taxes	843	1,182
Allowance for equity funds used during construction	5,389	4,992
Other income (Note S-2)	1,783	415
Other expense (Note S-2)	(3,626)	(4,358)
Total	4,389	2,231
INTEREST DEDUCTIONS		
Interest on long-term debt	54,752	49,734
Interest on short-term borrowings	842	2,975
Debt discount, premium and expense	1,137	1,189
Allowance for borrowed funds used during construction	(3,019)	(3,724)
Total	53,712	50,174
NET INCOME (LOSS)	16,112	(10,829)
Less: Net income attributable to noncontrolling interests (Note 9)	5,128	4,650
NET INCOME (LOSS) ATTRIBUTABLE TO COMMON SHAREHOLDER	$ 10,984	$ (15,479)

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

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

	March 31, 2010	December 31, 2009
ASSETS		
UTILITY PLANT		
Electric plant in service and held for future use	$ 12,781,326	$ 12,781,256
Less accumulated depreciation and amortization	4,335,052	4,326,908
Net	8,446,274	8,454,348
Construction work in progress	521,980	460,748
Palo Verde sale leaseback, net of accumulated depreciation (Note 9)	144,528	146,722
Intangible assets, net of accumulated amortization	169,726	164,183
Nuclear fuel, net of accumulated amortization	142,254	118,243
Total utility plant	9,424,762	9,344,244
INVESTMENTS AND OTHER ASSETS		
Nuclear decommissioning trust (Note 18)	433,399	414,576
Assets from risk management activities (Note 10)	40,763	28,855
Other assets	70,478	68,839
Total investments and other assets	544,640	512,270
CURRENT ASSETS		
Cash and cash equivalents	1,644	120,798
Customer and other receivables	197,921	280,226
Accrued unbilled revenues	86,466	110,971
Allowance for doubtful accounts	(5,810)	(6,063)
Materials and supplies (at average cost)	171,118	176,020
Fossil fuel (at average cost)	37,907	39,245
Assets from risk management activities (Note 10)	75,421	50,619
Deferred income taxes	77,915	53,990
Other current assets	34,223	25,724
Total current assets	676,805	851,530
DEFERRED DEBITS		
Regulatory assets	863,233	813,161
Income tax receivable	65,498	65,498
Unamortized debt issue costs	20,395	20,959
Other	80,311	73,909
Total deferred debits	1,029,437	973,527
TOTAL ASSETS	$ 11,675,644	$ 11,681,571

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

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

	March 31, 2010	December 31, 2009
LIABILITIES AND EQUITY		
CAPITALIZATION		
Common stock	$ 178,162	$ 178,162
Additional paid-in capital	2,126,863	2,126,863
Retained earnings	1,218,610	1,250,126
Accumulated other comprehensive loss:		
Pension and other postretirement benefits	(28,469)	(29,114)
Derivative instruments	(128,180)	(80,682)
Total APS shareholder equity (Note S-1)	3,366,986	3,445,355
Noncontrolling interest (Note 9)	87,452	82,324
Total equity	3,454,438	3,527,679
Long-term debt less current maturities (Note 4)	3,180,434	3,180,406
Palo Verde sale leaseback lessor notes (Notes 4 and 9)	126,000	126,000
Total capitalization	6,760,872	6,834,085
CURRENT LIABILITIES		
Short-term borrowings	195,000	—
Current maturities of long-term debt (Note 4)	222,825	222,959
Accounts payable	194,143	213,833
Accrued taxes (Note 8)	132,055	158,051
Accrued interest	52,499	54,099
Customer deposits	70,302	70,780
Liabilities from risk management activities (Note 10)	52,469	55,908
Other current liabilities	91,459	124,995
Total current liabilities	1,010,752	900,625
DEFERRED CREDITS AND OTHER		
Deferred income taxes	1,666,281	1,582,945
Deferred fuel and purchased power regulatory liability (Note 5)	105,378	87,291
Other regulatory liabilities	670,023	679,072
Liability for asset retirements	306,868	301,783
Liabilities for pension and other postretirement benefits (Note 6)	682,595	766,378
Customer advances for construction	134,030	136,595
Liabilities from risk management activities (Note 10)	79,194	62,443
Coal mine reclamation	92,303	92,060
Unrecognized tax benefits (Note 8)	75,202	140,638
Other	92,146	97,656
Total deferred credits and other	3,904,020	3,946,861
COMMITMENTS AND CONTINGENCIES (SEE NOTES)		
TOTAL LIABILITIES AND EQUITY	$ 11,675,644	$ 11,681,571

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

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

	Three Months Ended March 31,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income (Loss)	$ 16,112	$ (10,829)
Adjustments to reconcile net income (loss) to net cash used for operating activities:		
Depreciation and amortization including nuclear fuel	113,195	110,089
Deferred fuel and purchased power	44,040	28,238
Deferred fuel and purchased power amortization	(25,953)	28,961
Allowance for equity funds used during construction	(5,389)	(4,992)
Deferred income taxes	47,754	(6,335)
Change in mark-to-market valuations	1,842	3,823
Changes in current assets and liabilities:		
Customer and other receivables	61,239	71,551
Accrued unbilled revenues	24,505	15,365
Materials, supplies and fossil fuel	6,240	(11,796)
Other current assets	(8,499)	(2,042)
Accounts payable	(22,275)	(70,828)
Accrued taxes	(25,996)	17,371
Other current liabilities	(35,614)	(43,964)
Change in margin and collateral accounts — assets	(11,280)	(23,876)
Change in margin and collateral accounts — liabilities	(124,495)	(162,012)
Change in unrecognized tax benefits	(61,683)	(797)
Change in other long-term assets	(23,033)	(1,165)
Change in other long-term liabilities	(34,918)	19,797
Net cash flow used for operating activities	(64,208)	(43,441)
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(199,276)	(188,973)
Contributions in aid of construction	2,949	18,762
Capitalized interest	(3,019)	(3,724)
Proceeds from nuclear decommissioning trust sales	158,448	129,816
Investment in nuclear decommissioning trust	(164,552)	(135,264)
Other	(1,639)	1,500
Net cash flow used for investing activities	(207,089)	(177,883)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	—	496,475
Repayment and reacquisition of long-term debt	(357)	(233)
Short-term borrowings-net	195,000	(285,508)
Dividends paid on common stock	(42,500)	(42,500)
Net cash flow provided by financing activities	152,143	168,234
NET DECREASE IN CASH AND CASH EQUIVALENTS	(119,154)	(53,090)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	120,798	71,544
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 1,644	$ 18,454
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Income taxes, net of refunds	$ 65,498	$ 13,704
Interest, net of amounts capitalized	$ 54,174	$ 40,867

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

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

	Condensed Consolidated Footnote Reference	APS' Supplemental Footnote Reference
Consolidation and Nature of Operations	Note 1	—
Condensed Consolidated Financial Statements	Note 2	—
Quarterly Fluctuations	Note 3	—
Long-term Debt and Liquidity Matters	Note 4	—
Regulatory Matters	Note 5	—
Retirement Plans and Other Benefits	Note 6	—
Business Segments	Note 7	—
Income Taxes	Note 8	—
Variable Interest Entities	Note 9	—
Derivative and Energy Trading Accounting	Note 10	—
Changes in Equity	Note 11	Note S-1
Commitments and Contingencies	Note 12	—
Nuclear Insurance	Note 13	—
Other Income and Other Expense	Note 14	Note S-2
Guarantees	Note 15	—
Earnings Per Share	Note 16	—
Discontinued Operations	Note 17	—
Nuclear Decommissioning Trust	Note 18	—
Fair Value Measurements	Note 19	—
Real Estate Impairment Charge	Note 20	—

ARIZONA PUBLIC SERVICE COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

S-1. Changes in Equity

The following tables show APS' changes in shareholder equity and changes in equity of noncontrolling interests for the three months ended March 31, 2010 and 2009 (dollars in thousands):

	Three Months Ended March 31, 2010			Three Months Ended March 31, 2009		
	Shareholder Equity	Noncontrolling Interests	Total	Shareholder Equity	Noncontrolling Interests	Total
Beginning balance, January 1	$ 3,445,355	$ 82,324	$3,527,679	$ 3,339,150	$ 77,601	$3,416,751
Net income (loss)	10,984	5,128	16,112	(15,479)	4,650	(10,829)
Other comprehensive loss:						
Net unrealized losses on derivative instruments (a)	(91,667)	—	(91,667)	(138,548)	—	(138,548)
Net reclassification of realized losses to income (b)	13,185	—	13,185	25,365	—	25,365
Reclassification of pension and other postretirement benefits to income	1,064	—	1,064	987	—	987
Income tax benefit related to items of other comprehensive income	30,565	—	30,565	44,363	—	44,363
Total other comprehensive loss	(46,853)	—	(46,853)	(67,833)	—	(67,833)
Total comprehensive income (loss)	(35,869)	5,128	(30,741)	(83,312)	4,650	(78,662)
Common stock dividends	(42,500)	—	(42,500)	(42,500)	—	(42,500)
Other	—	—	—	4,503	—	4,503
Ending balance, March 31	$ 3,366,986	$ 87,452	$3,454,438	$ 3,217,841	$ 82,251	$3,300,092

(a) These amounts primarily include unrealized gains and losses on contracts used to hedge our forecasted electricity and natural gas requirements to serve Native Load. These changes are primarily due to changes in forward natural gas prices and wholesale electricity prices.

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

ARIZONA PUBLIC SERVICE COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

S-2. Other Income and Other Expense

The following table provides detail of APS' other income and other expense for the three months ended March 31, 2010 and 2009 (dollars in thousands):

	Three Months Ended March 31,	
	2010	2009
Other income:		
Interest income	$ 462	$ 183
Investment gains — net	1,165	—
Miscellaneous	156	232
Total other income	$ 1,783	$ 415
Other expense:		
Non-operating costs (a)	$ (1,958)	$ (1,335)
Asset dispositions	(39)	(83)
Investment losses — net	—	(1,323)
Miscellaneous	(1,629)	(1,617)
Total other expense	$ (3,626)	$ (4,358)

(a) As defined by the FERC, includes below-the-line non-operating utility income and expense (items excluded from utility rate recovery).

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

INTRODUCTION

The following discussion should be read in conjunction with Pinnacle West's Condensed Consolidated Financial Statements and Arizona Public Service Company's Condensed Consolidated Financial Statements and the related Notes that appear in Item 1 of this report. For purposes of this report, a "Note" refers to a Note to Pinnacle West's Condensed Consolidated Financial Statements in Item 1 of this report. For information on the broad factors that may cause our actual future results to differ from those we currently seek or anticipate, see "Forward-Looking Statements" at the front of this report and "Risk Factors" in Item 1A of the 2009 Form 10-K.

OVERVIEW

Pinnacle West owns all of the outstanding common stock of APS. APS is a vertically-integrated electric utility that provides retail and wholesale electric service to most of the state of Arizona, with the major exceptions of about one-half of the Phoenix metropolitan area, the Tucson metropolitan area and Mohave County in northwestern Arizona. APS accounts for substantially all of our revenues and earnings, and is expected to continue to do so.

Areas of Business Focus

Operations

Nuclear. APS operates and is a joint-owner of the Palo Verde Nuclear Generating Station. With a focus on safely and efficiently generating electricity for the long-term, APS applied for twenty-year renewals of its operating licenses for each of the three Palo Verde units, and is making preparations to secure necessary resources to operate the plant during this extended period of time. In April 2010, APS signed an agreement on behalf of the Palo Verde participants with five cities to provide cooling water essential to power production at Palo Verde for the next forty years.

Coal and Related Environmental Matters. APS is a joint-owner of three coal-fired power plants and acts as operating agent for two of the plants. APS is focused on developing legislation and increased regulation concerning greenhouse gas emissions, and the potential impacts on its coal fleet. Recent concern over climate change and other emission-related issues could have a significant impact on APS' capital expenditures and operating costs in the form of taxes, emissions allowances or required equipment upgrades for these plants. APS is closely monitoring its long range capital management plans, understanding that the resulting legislation and regulation could impact the economic viability of certain plants, as well as the willingness or ability of power plant participants to fund any such equipment upgrades. In particular, Southern California Edison, a participant in the Four Corners Power Plant ("Four Corners"), has indicated that certain California legislation may prohibit it from making emission control expenditures at the plant.

Transmission and Delivery. APS' 2010 transmission plan projects that it will invest approximately $520 million in new transmission over the next ten years, which includes 270 miles of new lines. APS is working closely with regulators to identify and plan for transmission needs resulting from the current focus on renewable energy. APS is also working to establish and expand smart grid technology throughout its service territory designed to provide a variety of benefits both to APS and its customers. This technology is designed to allow customers to better monitor their energy use and needs, minimize system outage durations and the number of customers that experience outages, and facilitate cost savings to APS through improved reliability and the automation of certain distribution functions, including remote meter reading and remote connects and disconnects.

Renewable Energy. APS is committed to increasing the amount of energy produced by renewable energy resources. The ACC adopted a renewable energy standard several years ago, recognizing the importance of renewable energy to our state. In the Settlement Agreement for the 2008 general retail rate case, APS agreed to exceed these standards, committing that approximately 10% of APS' energy will come from renewable resources by the year 2015. A variety of other provisions in the Settlement Agreement reinforce APS' dedication to renewable energy through initiatives such as building photovoltaic solar plants, installing solar rooftop panels on schools and government buildings and seeking an Arizona wind generation project.

On March 3, 2010, the ACC approved the AZ Sun program, under which APS plans to own 100 MW of photovoltaic power plants across Arizona by investing up to $500 million through 2014. These projects will be purchased upon completion from developers that will be selected through competitive procurement processes to build the plants. APS currently anticipates that this solar capacity would be placed into service in the 2011 to 2014 timeframe. The ultimate timing depends on the outcome of current and future procurement processes. See Note 5 for additional details of this program, including the related cost recovery. APS also issued two requests for proposal ("RFP") for renewable resources in early 2010. These RFPs are part of the process for procuring the additional renewable resources required under the rate case settlement. The first RFP is for utility-scale solar photovoltaic projects between 15 and 50 MW. This RFP serves as the first procurement step for implementing the AZ Sun program. The second RFP is for wind projects between 15 and 100 MW to be located within Arizona.

Rate Matters. APS needs timely recovery through rates of its capital and operating expenditures to maintain adequate financial health. APS' retail rates are regulated by the ACC and its wholesale electric rates (primarily for transmission) are regulated by the FERC. At the end of 2009, the ACC approved a settlement agreement entered into by APS and twenty-one of the twenty-three other parties to APS' general retail rate case, with modifications that did not materially affect the overall economic terms of the agreement. The rate case settlement should strengthen APS' financial condition by allowing for rate stability and a greater level of cost recovery and return on investment. It also authorizes and requires equity infusions into APS of at least $700 million prior to the end of 2014. The settlement demonstrates cooperation among APS, the ACC staff, the Residential Utility Consumer Office (RUCO) and other intervenors to the rate case, and establishes a future rate case filing plan that allows APS the opportunity to help shape Arizona's energy future outside of continual rate cases. See Note 5 for a discussion of the Settlement Agreement terms and information on APS' FERC rates.

APS has several recovery mechanisms in place that provide more timely recovery to APS of its fuel and transmission costs, and costs associated with the promotion and implementation of its energy efficiency, demand-side management and renewable energy efforts and customer programs. These mechanisms are described more fully in Note 5.

Financial Strength and Flexibility. Pinnacle West and APS currently have ample borrowing capacity under their respective credit facilities and have been able to access these facilities, ensuring adequate liquidity for each company. In early February 2010, APS entered into a $500 million revolving credit facility, replacing its $377 million revolving credit facility that would have otherwise terminated in December 2010. At that same time, Pinnacle West entered into a $200 million revolving credit facility that replaces its $283 million facility that also would have otherwise terminated in December 2010. Pinnacle West and APS also accessed the commercial paper markets, which neither company had utilized since the third quarter of 2008 due to negative market conditions.

In April 2010, we issued 6,900,000 shares of common stock at an offering price of $38.00 per share, resulting in net proceeds of approximately $253 million. Pinnacle West contributed all of the proceeds from this offering to APS. APS anticipates using these capital contributions to repay short-term indebtedness, to finance capital expenditures and for other general corporate purposes.

SunCor Real Estate Operations. As a result of the distressed conditions in the real estate markets, during 2009 SunCor undertook a program to dispose of its homebuilding operations, master-planned communities, land parcels, commercial assets and golf courses in order to reduce its outstanding debt. As a result, during 2009, we recorded impairment charges of approximately $266 million pre-tax and $161 million after income taxes. In the first quarter of 2010, we recorded impairment charges of approximately $15 million pre-tax and $9 million after income taxes. See "Pinnacle West Consolidated – Liquidity and Capital Resources – Other Subsidiaries – SunCor" below for a discussion of SunCor's outstanding debt and related matters and Note 20 for a further discussion of impairment charges.

Subsidiaries. The operations of our other first tier subsidiaries, El Dorado and APSES, are not expected to have any material impact on our financial results, or to require any material amounts of capital, over the next three years.

Key Financial Drivers

In addition to the continuing impact of the matters described above, many factors influence our financial results and our future financial outlook, including those listed below. We closely monitor these factors to plan for the Company's current needs, and to adjust our expectations, financial budgets and forecasts appropriately.

Regulated Electricity Segment Revenues. For the years 2007 through 2009, retail electric revenues comprised approximately 94% of our total electric operating revenues. Our electric operating revenues are affected by customer growth, variations in weather from period to period, customer mix, average usage per customer and the impacts of energy efficiency programs, electricity rates and tariffs, the recovery of PSA deferrals and the operation of other recovery mechanisms. Off-system sales of excess generation output, purchased power and natural gas are included in regulated electricity segment revenues and related fuel and purchased power because they are credited to APS' retail customers through the PSA. These revenue transactions are affected by the availability of excess generation or other energy resources and wholesale market conditions, including competition, demand and prices.

Customer and Sales Growth. Customer growth in APS' service territory for the three-month period ended March 31, 2010 was 0.6% compared with the prior year period. For the three years 2007 through 2009, APS' customer growth averaged 1.8% per year. We currently expect annual customer growth to average about 1% for 2010 through 2012 due to economic conditions both nationally and in Arizona. Retail sales in kilowatt-hours, adjusted to exclude the effects of weather variations, for the three-month period ended March 31, 2010 declined 1.7% compared to the same period in the prior year, reflecting the poor economic conditions and the effects of our energy efficiency programs. For the three years 2007 through 2009, APS' actual retail electricity sales in kilowatt-hours, adjusted to exclude the effects of weather variations, grew at an average annual rate of 0.2%. We currently estimate that total annual retail electricity sales in kilowatt-hours will remain flat on average during 2010 through 2012, including the effects of APS' energy efficiency programs, but excluding the effects of weather variations. A continuation of the economic downturn, or the failure of the Arizona economy to rebound in the near future, could further impact these estimates. The customer and sales growth referred to in this paragraph apply to Native Load customers.

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

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

Fuel and Purchased Power Costs. Fuel and purchased power costs included on our Condensed Consolidated Statements of Income are impacted by our electricity sales volumes, existing contracts for purchased power and generation fuel, our power plant performance, transmission availability or constraints, prevailing market prices, new generating plants being placed in service in our market areas, our hedging program for managing such costs and PSA deferrals and the amortization thereof.

Operations and Maintenance Expenses. Operations and maintenance expenses are impacted by growth, power plant operations, maintenance of utility plant (including generation, transmission, and distribution facilities), inflation, outages, higher-trending pension and other postretirement benefit costs, renewable energy and demand side management related expenses (which are offset by the same amount of regulated electricity segment operating revenues) and other factors. In its recent retail rate case settlement, APS committed to operational expense reductions from 2010 through 2014 and received approval to defer certain pension and other postretirement benefit cost increases to be incurred in 2011 and 2012.

Depreciation and Amortization Expenses. Depreciation and amortization expenses are impacted by net additions to utility plant and other property (such as new generation, transmission, and distribution facilities), and changes in depreciation and amortization rates. The “Capital Expenditures” section below provides information regarding the planned additions to our facilities. We have also applied to the NRC for renewed operating licenses for each of the Palo Verde units. If the NRC grants the extension, we estimate that our annual pretax depreciation expense will decrease by approximately $34 million at the later of the license extension date or January 1, 2012.

Property Taxes. Taxes other than income taxes consist primarily of property taxes, which are affected by the value of property in-service and under construction, assessment ratios, and tax rates. The average property tax rate for APS, which currently owns the majority of our property, was 7.5% of the assessed value for 2009 and 7.8% of the assessed value for 2008. We expect property taxes to increase as we add new utility plant (including new generation, transmission and distribution facilities described below under “Capital Additions”) and as we improve our existing facilities.

Income Taxes. Income taxes are affected by the amount of pre-tax book income, income tax rates, and certain non-taxable items, such as the allowance for equity funds used during construction. In addition, income taxes may also be affected by the settlement of issues with taxing authorities.

Interest Expense. Interest expense is affected by the amount of debt outstanding and the interest rates on that debt (see Note 4.) The primary factors affecting borrowing levels are expected to be our capital expenditures, long-term debt maturities, and internally generated cash flow. Capitalized interest offsets a portion of interest expense while capital projects are under construction. We stop accruing capitalized interest on a project when it is placed in commercial operation.

PINNACLE WEST CONSOLIDATED — RESULTS OF OPERATIONS

Our results of operations, provided below, are based upon our two reportable business segments:

- our regulated electricity segment, which consists of traditional regulated retail and wholesale electricity businesses (primarily retail and wholesale sales supplied to traditional cost-based rate regulation ("Native Load") customers) and related activities and includes electricity generation, transmission and distribution; and
- our real estate segment, which consists of SunCor's real estate development and investment activities.

Operating Results — Three-month period ended March 31, 2010 compared with three-month period ended March 31, 2009

Our consolidated net loss attributable to common shareholders for the three months ended March 31, 2010 was $6 million, compared with a net loss of $157 million for the comparable prior-year period. The improved results were primarily due to lower real estate impairment charges recorded in 2010 compared with the prior-year period by SunCor, the Company's real estate subsidiary.

In addition, regulated electricity segment net income increased approximately $27 million from the prior-year period primarily due to increased revenues related to APS' retail rate increases.

The following table presents net income (loss) attributable to common shareholders by business segment compared with the prior-year period:

	Three Months Ended March 31,		Increase (Decrease) in Net Income Attributable to Common Shareholders
	2010	2009	
	(dollars in millions)		
Regulated Electricity Segment:			
Operating revenues less fuel and purchased power expenses	$ 396	$ 355	$ 41
Operations and maintenance	(207)	(194)	(13)
Depreciation and amortization	(101)	(100)	(1)
Taxes other than income taxes	(32)	(34)	2
Other income (expenses), net	—	(4)	4
Interest charges, net of capitalized financing costs	(52)	(48)	(4)
Income taxes	8	10	(2)
Noncontrolling interests (Note 9)	(5)	(5)	—
Regulated electricity segment net income (loss)	7	(20)	27
Real Estate Segment:			
Real estate impairment charges (Note 20)	(15)	(202)	187
Other real estate operations	(6)	(15)	9
Income taxes	8	85	(77)
Real estate segment net loss	(13)	(132)	119
All other (a)	—	(5)	5
Net Loss Attributable to Common Shareholders	$ (6)	$ (157)	$ 151

(a) Includes activities related to APSES and El Dorado. None of the activities of either of these companies constitutes a reportable segment.

Regulated electricity segment

This section includes a discussion of major variances in income and expense amounts for the regulated electricity segment.

Operating revenues less fuel and purchased power expenses

Regulated electricity segment operating revenues less fuel and purchased power expenses were $41 million higher for the three months ended March 31, 2010 compared with the prior-year period. The following table describes the major components of this change:

	Increase (Decrease)		
	Operating revenues	Purchased power and fuel expenses	Net change
	(dollars in millions)		
Retail regulatory settlement effective January 1, 2010:			
Retail base rate increases, net of deferrals	$ 51	$ 27	$ 24
Line extension revenues (Note 5)	5		5
Transmission rate increases	4		4
Higher demand-side management surcharges (substantially offset in operations and maintenance expense)	7		7
Lower retail revenues related to recovery of PSA deferrals, substantially offset by amortization of fuel and purchased power expense	(55)	(56)	1
Miscellaneous items, net	(3)	(3)	—
Total	$ 9	$ (32)	$ 41

Operations and maintenance Operations and maintenance expenses increased $13 million for the three months ended March 31, 2010 compared with the prior-year period primarily because of:

- An increase of $11 million related to higher labor expenses;
- An increase of $6 million related to demand-side management programs, which are primarily offset in operating revenues;
- A decrease of $8 million in generation costs, including timing of fossil-plant planned maintenance; and
- An increase of $4 million due to other miscellaneous factors.

Other income (expenses), net Other income (expenses), net, improved $4 million for the three months ended March 31, 2010 compared with the prior-year period primarily because of improved investment results. Other income (expenses), net, is comprised of the regulated electricity segment portions of the line items other income and other expense from the Condensed Consolidated Statements of Income.

Interest charges, net of capitalized financing costs Interest charges, net of capitalized financing costs increased $4 million for the three months ended March 31, 2010 compared with the prior-year period primarily because of higher debt balances. Interest charges, net of capitalized financing costs are comprised of the regulated electricity segment portions of the line items interest expense, capitalized interest and allowance for equity funds used during construction from the Condensed Consolidated Statements of Income.

Income taxes Income tax benefits were $2 million lower for the three months ended March 31, 2010 compared with the prior-year period primarily because of higher pretax income in the current-year period, partially offset by $8 million related to a reduction in the Company's 2010 effective income tax rate.

Real estate segment

During the first quarter of 2009, SunCor's Board of Directors authorized a series of strategic transactions to dispose of substantially all of SunCor's assets. This decision resulted in impairment charges of approximately $202 million pretax in the first quarter of 2009. The real estate segment net loss attributable to common shareholders was $119 million lower for the three months ended March 31, 2010 compared with the prior-year period primarily because of:

- A decrease in real estate impairment charges of $187 million;
- A decrease in the loss from other real estate operations of $9 million; and
- A decrease in income tax benefits of $77 million primarily because of a lower net loss for the 2010 period.

All Other

All other earnings were $5 million higher for the three months ended March 31, 2010 compared to the prior-year period primarily because of 2009 investment losses at El Dorado.

PINNACLE WEST CONSOLIDATED – LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

The following table presents net cash provided by (used for) operating, investing and financing activities for the three months ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Net cash flow used for operating activities	$ (14)	$ (56)
Net cash flow used for investing activities	(210)	(182)
Net cash flow provided by financing activities	82	166

The decrease of approximately $42 million in net cash used for operating activities is primarily due to decreased collateral and margin cash provided as a result of changes in commodity prices and other changes in working capital partially offset by a voluntary pension contribution in 2010 of approximately $100 million.

The increase of approximately $28 million in net cash used for investing activities is primarily due to higher levels of capital expenditures, net of related contributions in aid of construction (see table and discussion below).

The decrease of approximately $84 million in net cash provided by financing activities is primarily due to APS' issuance of $500 million of unsecured senior notes in 2009. This is partially offset by the reduction of short-term borrowings in 2009 and the incurrence of short-term borrowings in 2010.

Liquidity

Capital Expenditure Requirements

The following table summarizes the actual capital expenditures for the three months ended March 31, 2009 and 2010 and the estimated capital expenditures for the next three years:

CAPITAL EXPENDITURES
(dollars in millions)

	Three Months Ended March 31,		Estimated for the Year Ended December 31,		
	2009	2010	2010	2011	2012
APS Generation (a)	$ 60	$ 77	$ 309	$ 417	$ 520
Distribution	70	59	281	322	328
Transmission	31	36	145	161	192
Other (b)	5	11	84	71	48
Subtotal	166	183	819	971	1,088
Other	6	1	1	—	—
Total	$ 172	$ 184	$ 820	$ 971	$ 1,088

(a) Generation includes nuclear fuel expenditures of approximately $60 million to $80 million per year for 2010, 2011 and 2012.

(b) Primarily information systems and facilities projects.

Generation capital expenditures are comprised of various improvements to APS' existing fossil and nuclear plants. Examples of the types of projects included in this category are additions, upgrades and capital replacements of various power plant equipment, such as turbines, boilers and environmental equipment. Environmental expenditures for the years 2010, 2011 and 2012 are approximately $20 million, $80 million and $220 million, respectively. We are also monitoring the status of certain environmental matters, which, depending on their final outcome, could require modification to our environmental expenditures. (See "Business of Arizona Public Service Company – Environmental Matters – EPA Environmental Regulation – Regional Haze Rules and Mercury and other Hazardous Air Pollutants" in Item 1 of the 2009 Form 10-K.)

Distribution and transmission capital expenditures are comprised of infrastructure additions and upgrades, capital replacements, new customer construction and related information systems and facility costs. Examples of the types of projects included in the forecast include power lines, substations, line extensions to new residential and commercial developments and upgrades to customer information systems.

Capital expenditures will be funded with internally generated cash and external financings, which may include issuances of long-term debt and Pinnacle West common stock.

Pinnacle West (Parent Company)

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

On April 21, 2010, the Pinnacle West Board of Directors declared a quarterly dividend of $0.525 per share of common stock, payable on June 1, 2010, to shareholders of record on May 3, 2010.

An existing ACC order requires APS to maintain a common equity ratio of at least 40%. As defined in the ACC order, the common equity ratio is common equity divided by the sum of common equity and long-term debt, including current maturities of long-term debt. At March 31, 2010, APS' common equity ratio, as defined, was 50%. Its total common equity was approximately $3.4 billion, and total capitalization was approximately $6.7 billion. APS would be prohibited from paying dividends if the payment would reduce its common equity below approximately $2.7 billion, assuming APS' total capitalization remains the same.

Pinnacle West and APS maintain credit facilities in order to enhance liquidity and provide credit support. During the first quarter of 2010, Pinnacle West and APS refinanced existing revolving credit facilities that would have matured in December 2010. In addition, Pinnacle West and APS accessed the commercial paper market, which neither company had utilized since the third quarter of 2008 due to negative market conditions.

On February 12, 2010, Pinnacle West refinanced its $283 million revolving credit facility that would have matured in December 2010, and decreased the size of the facility to $200 million. The new facility matures February 2013. Pinnacle West has the option to increase the amount of the facility up to a maximum of $300 million upon the satisfaction of certain conditions and with the consent of the lenders. Pinnacle West will use the facility for general corporate purposes, repayment of long-term debt, commercial paper support and for the issuance of letters of credit. Interest rates are based on Pinnacle West's senior unsecured debt credit ratings. As a result of the downsized revolving credit facility, the Company also reduced the size of its commercial paper program to $200 million from $250 million.

At March 31, 2010, the $200 million revolver was available to support the issuance of up to $200 million in commercial paper or to be used as bank borrowings, including issuances of letters of credit up to $100 million. At March 31, 2010 the Company had outstanding $10 million of borrowings under its revolving credit facility and no letters of credit. In addition, Pinnacle West had commercial paper borrowings of $80 million at March 31, 2010.

In April 2010, Pinnacle West issued 6,900,000 shares of common stock at an offering price of $38.00 per share, resulting in net proceeds of approximately $253 million. Pinnacle West contributed all of the proceeds from this offering to APS. APS anticipates using these capital contributions to repay short-term indebtedness, to finance capital expenditures and for other general corporate purposes.

Pinnacle West expects to recognize approximately $131 million of cash tax benefits related to SunCor's strategic asset sales (see Note 20), which will not be fully realized until all the asset sale transactions are completed. Approximately $6 million of these benefits were recorded in the three months ended March 31, 2010 as reductions to income tax expense related to the current impairment charges. The additional $125 million of tax benefits were recorded as reductions to income tax expense related to SunCor impairment charges recorded on or before December 31, 2009.

The $85 million income tax receivable on the Condensed Consolidated Balance Sheets represents the anticipated refunds related to an APS tax accounting method change approved by the IRS in the third quarter of 2009 and the current year tax benefits related to the SunCor strategic asset sales that closed prior to March 31, 2010.

Pinnacle West sponsors a qualified defined benefit and account balance pension plan and a non-qualified supplemental excess benefit retirement plan for the employees of Pinnacle West and our subsidiaries. IRS regulations require us to contribute a minimum amount to the qualified plan. We contribute at least the minimum amount required under IRS regulations, but no more than the maximum tax-deductible amount. The minimum required funding takes into consideration the value of plan assets and our pension obligation. The assets in the plan are comprised of fixed-income, equity and short-term investments. Future year contribution amounts are dependent on plan asset performance and plan actuarial assumptions. We made no contribution to our pension plan in 2009. We currently estimate that our pension contributions could average around $100 million for several years, assuming the discount rate remains at approximately current levels. During the first quarter of 2010, we made a voluntary contribution of approximately $100 million to our pension plan. The contribution to our other postretirement benefit plans in 2010 is estimated to be approximately $15 million. APS and other subsidiaries fund their share of the contributions. APS' share is approximately 97% of both plans.

See Note 5 for information regarding the recent retail rate case settlement, which includes ACC authorization and requires equity infusions into APS of at least $700 million by December 31, 2014. Pinnacle West intends to issue equity to provide most of the funds for the equity infusions into APS. Such equity issuances may occur at any time in the period through 2014, in Pinnacle West's discretion.

APS

APS' capital requirements consist primarily of capital expenditures and mandatory redemptions of long-term debt. APS pays for its capital requirements with cash from operations and, to the extent necessary, equity infusions from Pinnacle West and external financings. See "Pinnacle West (Parent Company)" above for a discussion of the common equity ratio that APS must maintain in order to pay dividends to Pinnacle West.

On February 12, 2010, APS refinanced its $377 million revolving credit facility that would have matured in December 2010, and increased the size of the facility to $500 million. The new revolving credit facility terminates in February 2013. APS has the option to increase the amount of the facility up to a maximum of $700 million upon the satisfaction of certain conditions and with the consent of the lenders. APS will use the facility for general corporate purposes, commercial paper support and for the issuance of letters of credit. Interest rates are based on APS' senior unsecured debt credit ratings.

At March 31, 2010 APS had two committed revolving credit facilities totaling $989 million, including the $500 million credit facility described above and $489 million that terminates in September 2011. The revolvers are available either to support the issuance of up to $250 million in commercial paper or to be used for bank borrowings, including issuances of letters of credit up to $739 million. At March 31, 2010, APS had borrowings of $70 million under its $489 million credit facility and no letters of credit under its revolving credit facilities. APS had commercial paper borrowings of $125 million at March 31, 2010.

On January 1, 2010, due to the adoption of amended accounting guidance relating to VIEs, APS began consolidating the Palo Verde Lessor Trusts (see Note 9) and, as a result of consolidation of these VIEs, we have reported the Lessor Trusts' long-term debt on our Condensed Consolidated Balance Sheets. Interest rates on these debt instruments are 8%, and are fixed for the remaining life of the debt. As of March 31, 2010 approximately $26 million was classified as current maturities of long-term debt and $126 million was classified as long-term debt relating to these VIEs. These debt instruments mature on December 30, 2015 and have sinking fund features that are serviced by the lease payments. See Note 9 for additional discussion of the VIEs.

Other Financing Matters — See Note 5 for information regarding the PSA approved by the ACC. Although APS defers actual retail fuel and purchased power costs on a current basis, APS' recovery of the deferrals from its ratepayers is subject to annual and, if necessary, periodic PSA adjustments.

See Note 5 for information regarding the recent retail rate case settlement, which includes ACC authorization and requires equity infusions into APS of at least $700 million by December 31, 2014.

See Note 10 for information related to the change in our margin accounts.

Other Subsidiaries

The SunCor Secured Revolver is secured primarily by an interest in land, commercial properties and land contracts. At March 31, 2010, SunCor had outstanding borrowings of approximately $54 million under the SunCor Secured Revolver, which matured on January 30, 2010. SunCor and the lenders under the SunCor Secured Revolver have signed a forbearance agreement under which the lenders have agreed not to exercise any remedies prior to June 30, 2010 to allow time for SunCor to continue discussions concerning the potential sale of additional properties. In addition to the SunCor Secured Revolver, at March 31, 2010, SunCor had approximately $42 million of outstanding debt under other credit facilities ($26 million of which has matured and remains outstanding). To date, the lenders under these credit facilities have taken no enforcement action. At March 31, 2010, $92 million was classified as current maturities of long-term debt and $4 million was classified as short-term borrowings on our Condensed Consolidated Balance Sheets.

If SunCor is unable to obtain extensions or renewals of the SunCor Secured Revolver or its other matured debt, or if it is unable to comply with the mandatory repayment and other provisions of any new or modified credit agreements, SunCor could be required to immediately repay its outstanding indebtedness under all of its credit facilities as a result of cross-default provisions. Such an immediate repayment obligation would have a material adverse impact on SunCor's business and financial position and impair its ongoing viability.

SunCor cannot predict the outcome of negotiations with its lenders or its ability to sell assets for sufficient proceeds to repay its outstanding debt (see Note 20). SunCor's ability to generate sufficient cash from operations while it pursues lender negotiations and further asset sales is uncertain.

Neither Pinnacle West nor any of its other subsidiaries has guaranteed any SunCor indebtedness. A SunCor debt default would not result in a cross-default of any of the debt of Pinnacle West or any of its other subsidiaries. While there can be no assurances as to the ultimate outcome of this matter, Pinnacle West does not believe that SunCor's inability to obtain extensions or renewals from SunCor's lenders would have a material adverse impact on Pinnacle West's cash flows or liquidity.

As of March 31, 2010, SunCor could not transfer any cash dividends to Pinnacle West as a result of the covenants mentioned above. The restriction does not affect Pinnacle West's ability to meet its ongoing capital requirements.

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

APSES — APSES expects minimal capital expenditures over the next three years.

Debt Provisions

Pinnacle West's and APS' debt covenants related to their respective bank financing arrangements include maximum debt to capitalization ratios. Certain of APS' bank financing arrangements also include an interest coverage test. Pinnacle West and APS comply with these covenants and each anticipates it will continue to meet these and other significant covenant requirements. For both Pinnacle West and APS, these covenants require that the ratio of consolidated debt to total consolidated capitalization not exceed 65%. At March 31, 2010, the ratio was approximately 54% for Pinnacle West and 53% for APS. The provisions regarding interest coverage require minimum cash coverage of two times the interest requirements for APS. The interest coverage was approximately 4.5 times under APS' bank financing agreements as of March 31, 2010. Failure to comply with such covenant levels would result in an event of default which, generally speaking, would require the immediate repayment of the debt subject to the covenants and could cross-default other debt. See further discussion of "cross-default" provisions below.

Neither Pinnacle West's nor APS' financing agreements contain "rating triggers" that would result in an acceleration of the required interest and principal payments in the event of a rating downgrade. However, our bank financial agreements contain a pricing grid in which the interest costs we pay are determined by our current credit ratings.

All of Pinnacle West's loan agreements contain "cross-default" provisions that would result in defaults and the potential acceleration of payment under these loan agreements if Pinnacle West or APS were to default under certain other material agreements. All of APS' bank agreements contain cross-default provisions that would result in defaults and the potential acceleration of payment under these bank agreements if APS were to default under certain other material agreements. Pinnacle West and APS do not have a material adverse change restriction for revolver borrowings.

See Note 4 for further discussions of liquidity matters.

Credit Ratings

The ratings of securities of Pinnacle West and APS as of May 5, 2010 are shown below. The ratings reflect the respective views of the rating agencies, from which an explanation of the significance of their ratings may be obtained. There is no assurance that these ratings will continue for any given period of time. The ratings may be revised or withdrawn entirely by the rating agencies if, in their respective judgments, circumstances so warrant. Any downward revision or withdrawal may adversely affect the market price of Pinnacle West's or APS' securities and serve to increase the cost of and limit access to capital. It may also require substantial additional cash or other collateral requirements related to certain derivative instruments, insurance policies, natural gas transportation, fuel supply, and other energy-related contracts. At this time, we believe we have sufficient liquidity to cover a downward revision to our credit ratings.

	Moody's	Standard & Poor's	Fitch
Pinnacle West			
Senior unsecured (a)	Baa3 (P)	BB+ (prelim)	N/A
Commercial paper	P-3	A-3	F3
Outlook	Stable	Stable	Negative
APS			
Senior unsecured	Baa2	BBB-	BBB
Secured lease obligation bonds	Baa2	BBB-	BBB
Commercial paper	P-2	A-3	F3
Outlook	Stable	Stable	Stable

(a) Pinnacle West has a shelf registration under SEC Rule 415. Pinnacle West currently has no outstanding, rated senior unsecured securities. However, Moody's assigned a provisional (P) rating and Standard & Poor's assigned a preliminary (prelim) rating to the senior unsecured securities that can be issued under such shelf registration.

Off-Balance Sheet Arrangements

On January 1, 2010 we adopted amended accounting guidance relating to VIEs and, as a result, we have consolidated certain entities which were previously not consolidated. The consolidation of these entities has impacted our consolidated financial statement results. See Note 9 for a discussion of these impacts.

Guarantees and Letters of Credit

We have issued parental guarantees and letters of credit and obtained surety bonds on behalf of our subsidiaries.

Our parental guarantees for APS relate to commodity energy products. In addition, Pinnacle West has obtained approximately $9 million of surety bonds related to APS' operations, which primarily relate to self-insured workers' compensation. Our credit support instruments enable APSES to offer energy-related products. Non-performance or non-payment under the original contract by our subsidiaries would require us to perform under the guarantee or surety bond. No liability is currently recorded on the Condensed Consolidated Balance Sheets related to Pinnacle West's current outstanding guarantees on behalf of our subsidiaries. At March 31, 2010, we had no guarantees that were in default. Our guarantees have no recourse or collateral provisions to allow us to recover amounts paid under the guarantees. We generally agree to indemnification provisions related to liabilities arising from or related to certain of our agreements, with limited exceptions depending on the particular agreement. See Note 15 for additional information regarding guarantees and letters of credit.

Contractual Obligations

Our future contractual obligations, including contingent obligations, related to purchased power and fuel contracts and renewable energy credits have increased from approximately $8.7 billion at December 31, 2009 to $9.2 billion at March 31, 2010 as follows (dollars in billions):

2010	2011-2012	2013-2014	Thereafter	Total
$ 0.5	$ 0.8	$ 1.0	$ 6.9	$ 9.2

These amounts have increased since the 2009 Form 10-K primarily due to increased solar contracts and renewable energy credits associated with the Renewable Energy Standard.

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

CRITICAL ACCOUNTING POLICIES

In preparing the financial statements in accordance with GAAP, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex, and actual results could differ from those estimates. There have been no changes to our critical accounting policies since our 2009 Form 10-K. See “Critical Accounting Policies” in Item 7 of the 2009 Form 10-K for further details about our critical accounting policies.

OTHER ACCOUNTING MATTERS

On January 1, 2010 we adopted amended accounting guidance relating to VIEs, and as a result we have consolidated certain entities which were previously not consolidated. The consolidation of these entities has impacted our consolidated financial statement results. See Note 9 for a discussion of these impacts.

MARKET AND CREDIT RISKS

Market Risks

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

Interest Rate and Equity Risk

We have exposure to changing interest rates. Changing interest rates will affect interest paid on variable-rate debt and the market value of fixed income securities held by our nuclear decommissioning trust fund (see Note 18). The nuclear decommissioning trust fund also has risks associated with the changing market value of its investments. Nuclear decommissioning costs are recovered in regulated electricity prices.

Commodity Price Risk

We are exposed to the impact of market fluctuations in the commodity price and transportation costs of electricity and natural gas. Our risk management committee, consisting of officers and key management personnel, oversees company-wide energy risk management activities to ensure compliance with our stated energy risk management policies. We manage risks associated with these market fluctuations by utilizing various commodity instruments that qualify as derivatives, including exchange-traded futures and options and over-the-counter forwards, options and swaps. As part of our risk management program, we use such instruments to hedge purchases and sales of electricity and fuels. The changes in market value of such contracts have a high correlation to price changes in the hedged commodities.

The following table shows the net pretax changes in mark-to-market of our derivative positions for the three months ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Mark-to-market of net positions at beginning of period	$ (169)	$ (282)
Recognized in earnings:		
Change in mark-to-market losses for future period deliveries	(3)	(6)
Mark-to-market losses realized including ineffectiveness during the period	1	2
Increase in regulatory asset	(31)	(40)
Recognized in OCI:		
Change in mark-to-market losses for future period deliveries (a)	(92)	(139)
Mark-to-market losses realized during the period	13	25
Change in valuation techniques	—	—
Mark-to-market of net positions at end of period	$ (281)	$ (440)

(a) The changes in mark-to-market recorded in OCI are due primarily to changes in forward natural gas prices.

The table below shows the fair value of maturities of our derivative contracts (dollars in millions) at March 31, 2010 by maturities and by the type of valuation that is performed to calculate the fair values. See Note 1, “Derivative Accounting” and “Fair Value Measurements,” in Item 8 of our 2009 Form 10-K and Note 19 for more discussion of our valuation methods.

Source of Fair Value	2010	2011	2012	2013	2014	Years thereafter	Total fair value
Prices actively quoted	$ (9)	$ (1)	$ —	$ —	$ —	$ —	$ (10)
Prices provided by other external sources	(121)	(93)	(23)	(3)	—	—	(240)
Prices based on models and other valuation methods	(8)	(4)	(1)	(5)	(5)	(8)	(31)
Total by maturity	$ (138)	$ (98)	$ (24)	$ (8)	$ (5)	$ (8)	$ (281)

The table below shows the impact that hypothetical price movements of 10% would have on the market value of our risk management assets and liabilities included on Pinnacle West's Condensed Consolidated Balance Sheets at March 31, 2010 and December 31, 2009 (dollars in millions):

	March 31, 2010 Gain (Loss)		December 31, 2009 Gain (Loss)	
	Price Up 10%	Price Down 10%	Price Up 10%	Price Down 10%
Mark-to-market changes reported in:				
Earnings				
Electricity	$ 1	$ (1)	$ 1	$ (1)
Natural gas	1	(1)	1	(1)
Regulatory asset, liability or OCI (a)				
Electricity	20	(20)	21	(21)
Natural gas	46	(46)	59	(59)
Total	$ 68	$ (68)	$ 82	$ (82)

(a) These contracts are hedges of our forecasted purchases of natural gas and electricity. The impact of these hypothetical price movements would substantially offset the impact that these same price movements would have on the physical exposures being hedged. To the extent the amounts are eligible for inclusion in the PSA, the amounts are recorded as either a regulatory asset or liability.

Credit Risk

We are exposed to losses in the event of non-performance or non-payment by counterparties. See Note 19 – "Fair Value Measurements" for a discussion of our credit valuation adjustment policy. See Note 10 for further discussion of credit risk.

ARIZONA PUBLIC SERVICE COMPANY – RESULTS OF OPERATIONS

Operating Results — Three-month period ended March 31, 2010 compared with three-month period ended March 31, 2009

APS' net income attributable to common shareholder for the three months ended March 31, 2010 was $11 million, compared with a net loss of $15 million for the comparable prior-year period. The improved results were primarily due to increased revenues related to APS' retail rate increases.

The following table presents net income (loss) attributable to common shareholder compared with the prior-year period:

	Three Months Ended March 31,		Increase (Decrease) in Net Income Attributable to Common Shareholder
	2010	2009	
	(dollars in millions)		
Operating revenues less fuel and purchased power expenses	$ 396	$ 355	$ 41
Operations and maintenance	(204)	(191)	(13)
Depreciation and amortization	(101)	(100)	(1)
Taxes other than income taxes	(31)	(34)	3
Other income (expenses), net	(2)	(3)	1
Interest charges, net of capitalized financing costs	(48)	(45)	(3)
Income taxes	6	8	(2)
Noncontrolling interests (Note 9)	(5)	(5)	—
Net income (loss) attributable to common shareholder	$ 11	$ (15)	$ 26

Operating revenues less fuel and purchased power expenses

Electric operating revenues less fuel and purchased power expenses were $41 million higher for the three months ended March 31, 2010 compared with the prior-year period. The following table describes the major components of this change:

	Increase (Decrease)		
	Operating revenues	Purchased power and fuel expenses	Net change
	(dollars in millions)		
Retail regulatory settlement effective January 1, 2010:			
Retail base rate increases, net of deferrals	$ 51	$ 27	$ 24
Line extension revenues (Note 5)	5		5
Transmission rate increases	4		4
Higher demand-side management surcharges (substantially offset in operations and maintenance expense)	7		7
Lower retail revenues related to recovery of PSA deferrals, substantially offset by amortization of fuel and purchased power expense	(55)	(56)	1
Miscellaneous items, net	(3)	(3)	—
Total	$ 9	$ (32)	$ 41

Operations and maintenance Operations and maintenance expenses increased $13 million for the three months ended March 31, 2010 compared with the prior-year period primarily because of:

- An increase of $11 million related to higher labor expenses;
- An increase of $6 million related to demand-side management programs, which are primarily offset in operating revenues;
- A decrease of $8 million in generation costs, including timing of fossil-plant planned maintenance; and
- An increase of $4 million due to other miscellaneous factors.

Interest charges, net of capitalized financing costs Interest charges, net of capitalized financing costs increased $3 million for the three months ended March 31, 2010 compared with the prior-year period primarily because of higher debt balances. Interest charges, net of capitalized financing costs are comprised of portions of the line items interest expense, allowance for borrowed funds used during construction and allowance for equity funds used during construction from the APS Condensed Consolidated Statements of Income.

Income taxes Income tax benefits were $2 million lower for the three months ended March 31, 2010 compared with the prior-year period primarily because of higher pretax income in the current-year period partially offset by $8 million related to a reduction in APS' 2010 effective income tax rate.

ARIZONA PUBLIC SERVICE COMPANY — LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

The following table presents net cash provided by (used for) operating, investing and financing activities for the three months ended March 31, 2010 and 2009 (dollars in millions):

	Three Months Ended March 31,	
	2010	2009
Net cash flow used for operating activities	$ (64)	$ (43)
Net cash flow used for investing activities	(207)	(178)
Net cash flow provided by financing activities	152	168

The increase of approximately $21 million in net cash used for operating activities is primarily due to the payment of income taxes and a voluntary pension contribution in 2010 of approximately $100 million, partially offset by decreased collateral and margin cash provided as a result of changes in commodity prices and other changes in working capital.

The increase of approximately $29 million in net cash used for investing activities is primarily due to higher levels of capital expenditures net of related contribution in aid of construction (see table and discussion above).

The decrease of approximately $16 million in net cash provided by financing activities is primarily due to APS' issuance of $500 million of unsecured senior notes in 2009. This is substantially offset by the reduction of short-term borrowings in 2009 and the incurrence of short-term borrowings in 2010.

Contractual Obligations

APS' future contractual obligations, including contingent obligations, related to purchased power and fuel contracts and renewable energy credits have increased from approximately $8.7 billion at December 31, 2009 to $9.2 billion at March 31, 2010 as follows (dollars in billions):

2010	2011-2012	2013-2014	Thereafter	Total
$ 0.5	$ 0.8	$ 1.0	$ 6.9	$ 9.2

These amounts have increased since the 2009 Form 10-K primarily due to increased solar contracts and renewable energy credits associated with the Renewable Energy Standard.

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

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See "Key Financial Drivers" and "Market and Credit Risks" in Item 2 above for a discussion of quantitative and qualitative disclosures about market risks.

Item 4. CONTROLS AND PROCEDURES

(a) Disclosure Controls and Procedures

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

Pinnacle West's management, with the participation of Pinnacle West's Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of Pinnacle West's disclosure controls and procedures as of March 31, 2010. Based on that evaluation, Pinnacle West's Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, Pinnacle West's disclosure controls and procedures were effective.

APS' management, with the participation of APS' Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of APS' disclosure controls and procedures as of March 31, 2010. Based on that evaluation, APS' Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, APS' disclosure controls and procedures were effective.

(b) Changes in Internal Control Over Financial Reporting

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

No change in Pinnacle West's or APS' internal control over financial reporting occurred during the fiscal quarter ended March 31, 2010 that materially affected, or is reasonably likely to materially affect, Pinnacle West's or APS' internal control over financial reporting.

Part II — OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

See “Environmental Matters” in Item 5 below and “Business of Arizona Public Service Company – Environmental Matters” in Item 1 of the 2009 Form 10-K in regard to pending or threatened litigation or other disputes.

See Note 12 with regard to a lawsuit brought by APS on behalf of itself and the other Palo Verde owners against the DOE, for information relating to FERC proceedings on California and Pacific Northwest energy market issues and for information regarding bankruptcy proceedings involving the landlord for our corporate headquarters building.

Item 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. – Risk Factors in the 2009 Form 10-K, which could materially affect the business, financial condition, cash flows or future results of Pinnacle West and APS. The risks described in the 2009 Form 10-K are not the only risks facing Pinnacle West and APS. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect the business, financial condition, cash flows and/or operating results of Pinnacle West and APS.

Item 5. OTHER INFORMATION

Construction and Financing Programs

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

Regulatory Matters

See Note 5 for a discussion of regulatory developments.

Environmental Matters

Superfund

See “Superfund” in Note 12 for a discussion of a Superfund site.

Climate Change

Legislative and Regulatory Initiatives. In the past several years, the United States Congress has considered bills that would regulate domestic greenhouse gas emissions. On June 26, 2009, the House of Representatives approved the American Clean Energy and Security Act of 2009, H.R. 2454. In addition to establishing clean energy programs, H.R. 2454 would establish a greenhouse gas emission cap-and-trade system starting in 2012 applicable to about 85% of all emission sources in the nation. A similar bill (Kerry-Boxer Bill, S. 1733) is pending before the Senate. Both of these bills would allocate a certain number of allowances to local distribution companies (such as APS) through 2030.

To the extent APS' emissions exceed the allowances allocated to it under these proposed bills, APS would have an "allowance gap." APS would have to purchase enough allowances from the market to fill these gaps. The table below illustrates the estimated cost impacts to APS in 2012 to acquire allowances to fill its allowance gap, and the associated retail rate impacts to customers under H.R. 2454 and S. 1733. For purposes of this illustration, the table provides three assumed allowance prices of $20, $50 and $75 per metric ton.

	H.R. 2454		S. 1733	
Allowance Cost ($ per metric ton)	Annual Cost ($ in millions)	Rate Impact	Annual Cost ($ in millions)	Rate Impact
$ 20	$ 68	2%	$ 101	3%
$ 50	$ 170	5%	$ 252	8%
$ 75	$ 255	8%	$ 379	12%

The actual economic and operational impact of this or any similar legislation on APS depends on a variety of factors, none of which can be fully known until such legislation passes and the specifics of the resulting program are established. These factors include the terms of the legislation with regard to allowed emissions; whether the permitted emissions allowances will be allocated to source operators free of cost or auctioned; the cost to reduce emissions or buy allowances in the marketplace; and the availability of offsets and mitigating factors to moderate the costs of compliance. At the present time, we cannot predict what form of legislation, if any, will ultimately pass.

In December 2009, the EPA determined that greenhouse gas emissions endanger public health and welfare. This determination was made in response to a 2007 United States Supreme Court ruling that greenhouse gases fit within the Clean Air Act's broad definition of "air pollutant" and, as a result, the EPA has the authority to regulate greenhouse gas emissions of new motor vehicles under the Clean Air Act. The endangerment finding could result in the EPA issuing new regulatory requirements under the Clean Air Act for new and modified major greenhouse gas emitting sources, including power plants. On September 30, 2009, the EPA announced a proposed rule under the Clean Air Act, known as the "tailoring rule," establishing new greenhouse gas emissions thresholds that determine when sources, including power plants, must obtain air operating permits or New Source Review permits. Several groups have filed lawsuits challenging the EPA's endangerment finding. At the present time we cannot predict whether the proposed tailoring rule will be adopted in its current or a revised form, what other rules or regulations may ultimately result from the EPA's finding, whether the parties challenging the endangerment finding will be successful, and what impact the proposed rule and potential other rules or regulations will have on APS' operations.

In anticipation of potential future regulation of greenhouse gases under the Clean Air Act as described above, on September 22, 2009, the EPA issued a mandatory greenhouse gas reporting rule. On March 10, 2010, the EPA proposed additions and amendments to the rule. The rule applies to direct greenhouse gas emissions from facilities such as APS' power plants. We expect that our incremental costs to comply with this rule will be immaterial since APS already routinely reports CO_2 and other greenhouse gas emissions from its plants.

In addition to federal legislative initiatives, state specific initiatives may also impact our business. While Arizona has not yet enacted any state specific legislation regarding greenhouse gas emissions, the California legislature enacted AB 32 and SB 1368 in 2006 to address greenhouse gas emissions and New Mexico is currently considering proposed legislation to address these issues. We are monitoring these and other state legislative developments to understand the extent to which they may affect our business, including our sales into the impacted states or the ability of our out-of-state power plant participants to continue their participation in certain coal-fired power plants. In particular, Southern California Edison, a participant in Four Corners, has indicated that SB 1368 may prohibit it from making emission control expenditures at the plant.

If any emission reduction legislation or regulations are enacted, we will assess our compliance alternatives, which may include replacement of existing equipment, installation of additional pollution control equipment, purchase of allowances, retirement or suspension of operations at certain coal-fired facilities, or other actions. Although associated capital expenditures or operating costs resulting from greenhouse gas emission regulations or legislation could be material, we believe that we would be able to recover the costs of these environmental compliance initiatives through our rates.

Regional Initiative. In 2007, six western states (Arizona, California, New Mexico, Oregon, Utah and Washington) and two Canadian provinces (British Columbia and Manitoba) entered into an accord, the Western Climate Initiative ("WCI"), to reduce greenhouse gas emissions from automobiles and certain industries, including utilities. Montana, Quebec and Ontario have also joined WCI. WCI participants set a goal of reducing greenhouse gas emissions 15% below 2005 levels by 2020. After soliciting public comment, in September 2008 WCI issued the design of a cap-and-trade program for greenhouse gas emissions. Due in part to the recent activity at the federal level discussed above, the initiative's momentum and the movement toward detailed proposed rules has slowed. On February 2, 2010, Arizona's Governor issued an executive order stating that Arizona will continue to be a member of WCI to monitor its advancements in this area, but it will not implement the WCI regional cap-and-trade program. As a result, while we continue to monitor the progress of WCI, at the present time we do not believe it will have a material impact on our operations.

Company Response to Climate Change Initiatives. We have undertaken a number of initiatives to address emission concerns, including renewable energy procurement and development, promotion of programs and rates that promote energy conservation, renewable energy use and energy efficiency, and implementation of an active technology innovation effort to evaluate potential emerging new technologies. APS currently has a diverse portfolio of renewable resources, including wind, geothermal, solar and biomass and we are focused on increasing the percentage of our energy that is produced by renewable resources.

On May 18, 2009, we submitted a comprehensive Climate Change Management Plan to the ACC to comply with an ACC order that directed APS to undertake a climate management plan, carbon emission reduction study and commitment and action plan with public input and ACC review. The Climate Change Management Plan details scientific, legislative and policy issues, potential physical and financial risks to APS, greenhouse gas emission inventory, APS technology innovation and greenhouse gas reduction efforts, and our companies' strategic approach to climate change management.

In January 2008, APS joined the Climate Registry as a Founding Reporter. Founding Reporters are companies that voluntarily joined the non-profit organization before May 2008 to measure and report greenhouse gas emissions in a common, accurate and transparent manner consistent across industry sectors and borders. Beginning in 2010, APS will no longer participate in the Climate Registry because it will be reporting substantially the same information under the new EPA reporting rule. Pinnacle West has also reported, and will continue to report, greenhouse gas emissions in its annual Corporate Responsibility Report, which is available on our website (*www.pinnaclewest.com*). In addition to emissions data, the report provides information related to the Company, its approach to sustainability and its workplace and environmental performance, as well as a copy of our Climate Change Management Plan discussed above. The information on Pinnacle West's website, including the Corporate Responsibility Report, is not incorporated by reference into this report.

Climate Change Lawsuits. In February 2008, the Native Village of Kivalina and the City of Kivalina, Alaska filed a lawsuit in federal court in the Northern District of California against nine oil companies, fourteen power companies (including Pinnacle West), and a coal company, alleging that the defendants' emissions of carbon dioxide contribute to global warming and constitute a public and private nuisance. The plaintiffs also allege that the effects of global warming will require the relocation of the village and they are seeking an unspecified amount of monetary damages. In June 2008, the defendants filed motions to dismiss the action, which were granted. The plaintiffs filed an appeal with the court in November 2009. We believe the action is without merit and intend to continue to defend against the claims.

Similar nuisance lawsuits are currently pending in the 2nd and 5th Circuits. In the fall of 2009, the U.S. Courts of Appeals for each of these Circuits reversed lower court decisions and ruled that the plaintiffs in both cases could bring common law nuisance lawsuits against coal-burning utilities allegedly contributing to global warming. Both cases, as well as the Kivalina case, raise political and legal considerations, including whether the courts can or should be making climate change policy decisions. We are not a party to either of these two lawsuits, but will monitor these developments and their potential industry impacts.

Coal Combustion Waste

On May 4, 2010, the EPA released its proposed regulations governing the handling and disposal of coal combustion byproducts ("CCBs"), such as fly ash and bottom ash. APS currently disposes of CCBs in ash ponds and dry storage areas at Cholla and Four Corners, and also sells a portion of its fly ash for beneficial reuse as a constituent in concrete production. The EPA proposes regulating CCBs as either non-hazardous waste or hazardous waste and is seeking comment on three different alternatives. The hazardous waste proposal would phase out the use of ash ponds for disposal of CCBs. The other two proposals regulate CCBs as non-hazardous waste and impose performance standards for ash disposal. One of these proposals would require retrofitting or closure of currently unlined ash ponds, while the other proposal would not require the installation of liners or pond closures. The EPA has not yet indicated a preference for any of the alternatives.

APS intends to file comments on the proposed rule during a 90-day comment period. We do not know when the EPA will issue a final rule, including required compliance dates. We cannot currently predict the outcome of the EPA's actions or whether such actions will have a material adverse impact on our financial position, results of operations or cash flows.

Item 6. EXHIBITS

(a) Exhibits

Exhibit No.	*Registrant(s)*	*Description*
10.1	Pinnacle West APS	Municipal Effluent Purchase and Sale Agreement dated April 29, 2010, by and between City of Phoenix, City of Mesa, City of Tempe, City of Scottsdale, City of Glendale, APS and Salt River Project Agricultural Improvement and Power District.
10.2	Pinnacle West APS	Reimbursement Agreement among APS, the Banks party thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent and Issuing Bank, dated as of April 16, 2010
10.3	Pinnacle West APS	Reimbursement Agreement among APS, the Banks party thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent and Issuing Bank, dated as of April 16, 2010
10.4	Pinnacle West	Letter Agreement dated May 21, 2009, between Pinnacle West Capital Corporation and David P. Falck
12.1	Pinnacle West	Ratio of Earnings to Fixed Charges
12.2	APS	Ratio of Earnings to Fixed Charges
12.3	Pinnacle West	Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividend Requirements
31.1	Pinnacle West	Certificate of Donald E. Brandt, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
31.2	Pinnacle West	Certificate of James R. Hatfield, Senior Vice President and Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended

Exhibit No.	*Registrant(s)*	*Description*
31.3	APS	Certificate of Donald E. Brandt, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
31.4	APS	Certificate of James R. Hatfield, Senior Vice President and Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
32.1	Pinnacle West	Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1850, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	APS	Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1850, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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

Exhibit No.	*Registrant(s)*	*Description*	*Previously Filed as Exhibit*[1]	*Date Filed*
3.1	Pinnacle West	Articles of Incorporation, restated as of May 21, 2008	3.1 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8-7-08
3.2	Pinnacle West	Pinnacle West Capital Corporation Bylaws, amended as of January 21, 2009	3.2 to Pinnacle West/APS December 31, 2008 Form 10-K Report, File Nos. 1-8962 and 1-4473	2-20-09
3.3	APS	Articles of Incorporation, restated as of May 25, 1988	4.2 to APS' Form S-3 Registration Nos. 33-33910 and 33-55248 by means of September 24, 1993 Form 8-K Report, File No. 1-4473	9-29-93
3.4	APS	Arizona Public Service Company Bylaws, amended as of December 16, 2008	3.4 to Pinnacle West/APS December 31, 2008 Form 10-K, File Nos. 1-8962 and 1-4473	2-20-09

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

SIGNATURES

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

PINNACLE WEST CAPITAL CORPORATION
(Registrant)

Dated: May 6, 2010

By: /s/ James R. Hatfield
James R. Hatfield
Sr. Vice President and Chief Financial Officer
(Principal Financial Officer and
Officer Duly Authorized to sign this Report)

ARIZONA PUBLIC SERVICE COMPANY
(Registrant)

Dated: May 6, 2010

By: /s/ James R. Hatfield
James R. Hatfield
Sr. Vice President and Chief Financial Officer
(Principal Financial Officer and
Officer Duly Authorized to sign this Report)

Exhibit 10.1

MUNICIPAL EFFLUENT PURCHASE AND SALE AGREEMENT

This MUNICIPAL EFFLUENT PURCHASE AND SALE AGREEMENT (this "Agreement") is entered by and between City of Phoenix ("Phoenix"), City of Mesa, City of Tempe, City of Scottsdale, and City of Glendale, Arizona municipal corporations (collectively the "Subregional Operating Group" and hereinafter referred to as the "SROG Cities" and individually as a "SROG City"); and Arizona Public Service Company, an Arizona corporation ("APS"), and Salt River Project Agricultural Improvement and Power District, an Arizona municipal corporation and agricultural improvement district ("SRP"), acting on behalf of themselves and El Paso Electric Company, a Texas corporation, Southern California Edison Company, a California corporation, Public Service Company of New Mexico, a New Mexico corporation, Southern California Public Power Authority, a California joint powers authority, and the Los Angeles Department of Water & Power, a municipal utility (hereinafter collectively referred to as the "Palo Verde Participants" and individually as a "Palo Verde Participant"). The SROG Cities and APS and SRP are sometimes individually referred to in this Agreement as a "Party" and collectively as the "Parties."

RECITALS

A. WHEREAS, on April 23, 1973, the SROG Cities, along with the Town of Youngtown, and APS and SRP entered into that certain "Option and Purchase of Effluent Agreement" referred to as "Agreement No. 13904" under which, among other things, the municipalities agreed to sell and deliver treated wastewater discharged from the 91st Avenue wastewater treatment plant ("Effluent"), a municipal wastewater treatment plant jointly owned by the SROG Cities (the "91st Avenue WWTP") and operated and maintained by Phoenix in its own behalf and as administrative agent for the other SROG Cities, for cooling use at the Palo Verde Nuclear Generating Station ("PVNGS") operated and maintained by APS in its own behalf and as administrative agent for the other Palo Verde Participants;

B. WHEREAS, on April 17, 1989, in *Arizona Public Service Co. v. Long*, 160 Ariz. 429 (1989), the Supreme Court of Arizona held, among other things, that municipal sewage effluent is neither surface water nor groundwater; it is water that loses its original character as surface water or groundwater, does not reestablish its legal character until it is returned to the ground as either surface water or groundwater, and prior to such return of effluent to the ground as either surface water or groundwater, the municipalities creating it are free to contract for the disposition of said effluent;

C. WHEREAS, the Effluent purchased and sold in accordance with the terms and conditions of this Agreement is intended by the Parties to meet the legal standards set forth in *Arizona Public Service Co. v. Long* regarding the SROG Cities' disposition of effluent;

D. WHEREAS, pursuant to the terms of Agreement No. 13904, the SROG Cities are committed to make available to the Palo Verde Participants up to 105,000 acre-feet of Effluent per year through June 1, 2025, 70,000 acre-feet of Effluent per year through April 24, 2026, and 35,000 acre-feet of Effluent per year through November 25, 2027, after which time Agreement No. 13904 would terminate;

E. WHEREAS, on December 11, 2008, APS, acting in its capacity as operating agent of PVNGS, submitted to the United States Nuclear Regulatory Commission three operating license renewal applications, which, if granted, will allow each of the three units at PVNGS to operate for an additional 20 years beyond the current license termination dates, thereby potentially extending the operating life of PVNGS through 2047;

F. WHEREAS, as a result of these PVNGS operating license extensions, the Palo Verde Participants desire to secure the right to continue purchasing and receiving Effluent from the SROG Cities through 2050;

G. WHEREAS, the Palo Verde Participants have determined that less than the entire 105,000 acre-foot quantity of Effluent the SROG Cities are committed to provide each year under Agreement No. 13904 is required to operate PVNGS at full capacity and, therefore, desire to reduce this quantity by 25,000 acre-feet per year;

H. WHEREAS, the SROG Cities desire to continue selling Effluent for beneficial use at PVNGS and any other electric generating facilities located within 10 miles of PVNGS pursuant to the terms and conditions contained in this Agreement;

I. WHEREAS, the extended sale and purchase of Effluent through 2050 will ensure the continued beneficial use of a renewable water source for power generation purposes while reducing the demand for non-renewable water supplies;

J. WHEREAS, this Agreement is intended to replace Agreement No. 13904, which will be of no further force and effect upon the Effective Date (defined in Section 2, below) of this Agreement; and

K. WHEREAS, APS and SRP are entering into this Agreement on their own behalf and on behalf of the other Palo Verde Participants pursuant to authorizations conferred on APS and SRP under that certain Arizona Nuclear Power Project Participation Agreement effective September 4, 1973, as such agreement is amended from time to time (the "ANPP Participation Agreement").

AGREEMENT

NOW, THEREFORE, in consideration of the mutual promises, terms, and conditions contained in this Agreement, and other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged by the Parties, the Parties agree as follows:

1. Ownership Changes.

1.1. As to the Palo Verde Participants. Any person, partnership, corporation, or governmental body or agency (each, a "Person") engaged in the generation, transmission, or distribution of energy that, after the Effective Date, becomes a Participant in PVNGS pursuant to Section 15 of the ANPP Participation Agreement shall be a Palo Verde Participant under this Agreement.

1.2. As to the SROG Cities. Any municipal corporation that, after the Effective Date, becomes the holder of an ownership interest in the 91st Avenue WWTP shall be a SROG City under this Agreement.

2. Term and Termination Date. This Agreement shall become effective on the date on which this Agreement has been approved by the governing bodies of all of the Parties and is signed by all of the Parties (the "Effective Date"), and shall terminate on December 31, 2050, unless extended by mutual agreement of the Parties pursuant to Section 14, below.

3. Effluent Deliveries; Quantity; Relinquishment.

3.1. Delivery Points. Throughout the term of this Agreement and in accordance with Section 3.2, below, Phoenix shall deliver up to 80,000 acre-feet of Effluent annually (the "Committed Quantity") to the delivery points (the "Delivery Points") interconnecting the 91st Avenue WWTP with the PVNGS water reclamation supply system pipeline (the "WRSS Pipeline") for transport to the PVNGS Water Reclamation Facility (the "PVNGS WRF"), which Delivery Points are depicted on **Exhibit "A"** attached to this Agreement. APS and Phoenix may from time to time, by mutual written agreement, designate additional points of delivery for the purpose of delivering Effluent to the WRSS Pipeline. Upon such designation, the new point of delivery shall become a Delivery Point under this Agreement.

3.2. Monthly Delivery Quantities.

3.2.1. Subject to Section 3.3, below, throughout the term of this Agreement, in each of the months from January through April and October through December, Phoenix shall make available for delivery to PVNGS up to 7,000 acre-feet of Effluent.

3.2.2. Subject to Section 3.3, below, throughout the term of this Agreement, in each of the months from May through September, Phoenix shall make available for delivery to PVNGS up to 8,000 acre-feet of Effluent.

3.3. Annual Delivery Quantities. Subject to Sections 3.5 and 7.2, below, Phoenix shall not be required to deliver more than the Committed Quantity of Effluent each calendar year under this Agreement.

3.4. Relinquishment of Portion of Committed Quantity.

3.4.1. The Palo Verde Participants may, upon six months' prior written notice to Phoenix, which notice shall be given in accordance with the requirements of Section 28.3, below (the "Relinquishment Notice"), permanently relinquish a portion of the Committed Quantity. The Relinquishment Notice shall identify the quantity of Effluent the Palo Verde Participants desire to relinquish (the "Relinquished Quantity") and the date on which the relinquishment shall become effective (the "Relinquishment Date").

Unless otherwise agreed to in writing by the SROG Cities, as of the date of the Relinquishment Notice, neither the Relinquished Quantity nor Relinquishment Date may be subsequently modified by the Palo Verde Participants, nor may the Palo Verde Participants rescind the relinquishment described in the Relinquishment Notice. Upon the Relinquishment Date, the Relinquished Quantity shall be deducted from the Committed Quantity in effect as of the date of the Relinquishment Notice, and the difference shall become the new Committed Quantity under this Agreement unless and until later modified pursuant to this Section 3.4.1.

3.4.2. Unless otherwise agreed to by the Parties, modifications to the Committed Quantity pursuant to this Section 3.4 shall not affect the monthly delivery requirements set forth in Section 3.2, above.

3.4.3. As of the Relinquishment Date, the Relinquished Quantity of Effluent shall be available for the SROG Cities' use, sale, or other disposition.

3.5. Substantial Change in Conditions. Section 3.4, above, notwithstanding, and subject to availability as reasonably in good faith determined and authorized by the SROG Cities, the Palo Verde Participants shall have the right to the delivery of additional quantities of Effluent for use consistent with the terms of this Agreement if certain conditions substantially change at PVNGS resulting in the need for additional Effluent. The additional quantities of Effluent resulting from substantially changed conditions pursuant to this Section 3.5 shall not be greater than 8,000 acre-feet per year during the term of this Agreement. The Per Acre-Foot Price (defined in Section 4.2, below) of any additional Effluent purchased by the Palo Verde Participants pursuant to this Section 3.5 shall be:

3.5.1. For calendar years 2010 through 2025, the Per Acre-Foot Price determined in accordance with Section 4.2.1, below;

3.5.2. For calendar years 2026 through 2050, the fourth tier Per Acre-Foot Price determined in accordance with Section 4.2.2, below.

4. Price. In consideration of the sale and delivery of Effluent from the SROG Cities throughout the term of this Agreement and the other services provided by the SROG Cities pursuant to this Agreement, the Palo Verde Participants shall make payments to Phoenix, on behalf of the SROG Cities, in the manner and as determined pursuant to this Section 4.

4.1. Water Supply Payments. The Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, four lump-sum payments of 7.5 million dollars each ("Water Supply Payments"), which Water Supply Payments shall total 30 million dollars. The Palo Verde Participants shall pay the Water Supply Payments in accordance with the following schedule:

4.1.1. Within 30 days after the Effective Date, 7.5 million dollars;

4.1.2. 7.5 million dollars by January 31 of each of the years 2011 through 2013;

4.1.3. Upon the Palo Verde Participants' full payment of 30 million dollars to the SROG Cities pursuant to this Section 4.1, no further Water Supply Payments shall be payable to the SROG Cities throughout the term of this Agreement.

4.2. Per Acre-Foot Payments. In addition to the Water Supply Payments described in Section 4.1, above, subject to Section 7.2, below, the Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, for each acre-foot of Effluent actually delivered to the Delivery Points pursuant to this Agreement ("Delivered Effluent Quantity"), as measured by the Metering Devices (defined in Section 6, below). Beginning on the Effective Date, throughout the term of this Agreement, the Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, for the previous month's Delivered Effluent Quantity by multiplying the previous month's Delivered Effluent Quantity by the applicable per acre-foot price (the product being the "Monthly Payment Amount"), as determined in accordance with Sections 4.2.1 and 4.2.2, below (the "Per Acre-Foot Price").

4.2.1. Per Acre-Foot Price: 2010 through 2025. For calendar years 2010 through 2025, the Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, the Per Acre-Foot Prices contained in the following schedule:

Contract Year	Per Acre-Foot Price
2010	$ 58.57
2011	$ 64.71
2012	$ 71.51
2013	$ 79.02
2014	$ 87.31
2015	$ 96.48
2016	$ 106.61
2017	$ 117.81
2018	$ 130.18
2019	$ 143.85
2020	$ 158.95
2021	$ 175.64
2022	$ 194.08
2023	$ 214.46
2024	$ 236.98
2025	$ 261.86

4.2.2. Per Acre-Foot Price: 2026 through 2050.

4.2.2.1. In calendar years 2026 through 2050, the Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, a Per Acre-Foot Price based on the following escalating tiered rate structure, which is composed of four price tiers based on the monthly Delivered Effluent Quantity:

Tier	Delivered Effluent Quantity
1	0 – 2,000 acre-feet
2	2,001 – 4,000 acre-feet
3	4,001 – 6,000 acre-feet
4	6,001 – 8,000 acre-feet

4.2.2.2. For each of the years 2026 through 2028, the Per Acre-Foot Prices applicable to Tiers 1 through 4 shall remain fixed at $198.00, $293.00, $349.00, and $474.00, respectively.

4.2.2.3. Starting in 2029 and every year thereafter through 2050, subject to an annual cap of three percent, the preceding year's Per Acre-Foot Price applicable to each tier shall be adjusted based on the simple average of the following three price indices as determined for that preceding calendar year: (i) Consumer Price Index — All Urban Consumers, U. S. City Average, Water and Sewerage Maintenance (not seasonally adjusted) [CUUR0000SEHG01)]; (ii) Consumer Price Index — All Urban Consumers, U.S. City Average, West Urban (not seasonally adjusted) [CUUR0400SA0, CUUS0400SA0]; and (iii) Consumer Price Index - All Urban Consumers, U.S. City Average, Electricity (not seasonally adjusted) [CUUR0000SEHF01, CUUS0000SEHF01] (the "Indices Basket"). Should any of the price indices in the Indices Basket be discontinued, the Parties shall substitute another such index generally recognized to be authoritative with respect to the subject matter of the discontinued index and this Agreement.

4.2.3. Monthly Billings and Payments. By the fifth business day of each month, APS shall provide to Phoenix the flow information necessary to calculate the Monthly Payment Amount, which flow information shall be sent by facsimile or electronic mail and regular United States Mail. Using the flow information provided by APS pursuant to this Section 4.2.3, Phoenix shall invoice APS for the Monthly Payment Amount by the fifteenth day of the same month in which the flow information was received from APS; and APS shall pay Phoenix, on behalf of the SROG Cities, the Monthly Payment Amount by the last day of that same month. Provided Phoenix

has properly invoiced APS pursuant to this Section 4.2.3, if APS fails to pay the Monthly Payment Amount by the due date thereof, Phoenix shall notify APS of such delinquent payment (the "Monthly Payment Delinquency Notice"), and APS shall pay the entire amount owed to Phoenix within 15 days after receipt of the Monthly Payment Delinquency Notice. If APS fails to pay the entire amount owed to Phoenix within 15 days of receipt of the Monthly Payment Delinquency Notice, beginning on the date on which the Monthly Payment Amount was originally due, interest shall accrue on the delinquent amount at a rate of one percent per month until paid.

5. Non-Usage Fees.

5.1. Calculation of Non-Usage Fee. Subject to Section 5.3, below, throughout the term of this Agreement, if APS does not take delivery of the entire Committed Quantity in a calendar year, in addition to any other payments owed to the SROG Cities pursuant to Section 4, above, the Palo Verde Participants shall pay a fee to Phoenix, on behalf of the SROG Cities, based on the difference between the Committed Quantity and Delivered Effluent Quantity in such year (the "Non-Usage Fee"). The Non-Usage Fee shall be calculated in accordance with the following schedule (*see* attached Appendix for illustrative examples of Non-Usage Fee calculations):

5.1.1. 2010 through 2025. For calendar years 2010 through 2025, the Non-Usage Fee shall be calculated by subtracting the Delivered Effluent Quantity in the calendar year (DQ) from the Committed Quantity in that same year (CQ) and multiplying the difference by 20 percent of the Per Acre-Foot Price (PP) applicable in that year (as determined in accordance with Section 4.2.1, above); or [(CQ – DQ) x PP x .20].

5.1.2. 2026 through 2050: Non-Extended Outage Periods. Subject to Section 5.1.3, below, for calendar years 2026 through 2050, the Non-Usage Fee shall be calculated by subtracting the Delivered Effluent Quantity in the calendar year (DQ) from the Committed Quantity in that same year (CQ) and multiplying the difference by 30 percent of the simple average per acre-foot price applicable in that year, which average per acre-foot price shall be determined by adding the Per Acre-Foot Price applicable to each of the four tiers in the relevant year, (as determined in accordance with Section 4.2.2, above) and dividing the total by four ("Average Per Acre-Foot Price" or (AP)); or [(CQ – DQ) x AP x ..30].

For example, because, in 2026, the Per Acre-Foot Prices for tiers 1 through 4 are set at $198, $293, $349, and $474, respectively, the Average Per Acre-Foot Price for these four tiers is $328.50. If 75,000 acre-feet (AF) of water was delivered to PVNGS in 2026 and the Committed Quantity was 80,000 acre-feet in that year, assuming there were no Extended Outage Periods (defined in Section 5.1.3.1, below), the Non-

Usage Fee payable to the SROG Cities by January 31, 2027 would be $492,750 ((80,000 AF – 75,000 AF) x $328.50 x .30).

5.1.3. 2026 through 2050: Extended Outage Periods. For calendar years 2026 through 2050, in lieu of the formula set forth in Section 5.1.2, above, if any PVNGS electric generating unit is shut down ("Outage Unit") for an Extended Outage Period (defined in Section 5.1.3.1, below), the Non-Usage Fee applicable to each Outage Unit during the Extended Outage Period only shall be determined by using the "Representative Usage" (defined in Section 5.1.3.2, below) of such unit. The Non-Usage Fee payable for each Outage Unit during the Extended Outage Period shall be calculated by multiplying the Representative Usage (RU) by 20 percent of the Average Per Acre-Foot Price (AP) applicable in that year; or [RU x AP x .20].

5.1.3.1. "Extended Outage Period" shall mean a period of 90 or more consecutive days over which a PVNGS electric generating unit is shut down. The Extended Outage Period shall commence on the day the electric generating unit is shut down and shall terminate on the day the electric generating unit has resumed full power generation. For purposes of this Section 5, "full power" means operation of a PVNGS electric generating unit at or near maximum generation with consideration for ambient temperature, regulatory requirements, and equipment conditions.

5.1.3.2. "Representative Usage" is an estimate of the quantity of Effluent the Outage Unit would have used had it not experienced an Extended Outage Period, and is necessary to calculate the Non-Usage Fee for that Extended Outage Period. The Representative Usage shall equal the average Effluent usage over the entirety of the Extended Outage Period of the two remaining PVNGS electric generating units that operated at full power during such period. If only one PVNGS electric generating unit operated at full power during the entirety of the Extended Outage Period, the Representative Usage shall equal the Effluent usage of that unit over such period. If none of the PVNGS electric generating units operated at full power over the entirety of the Extended Outage Period, the Representative Usage shall be determined by considering the Effluent usage during the most recent year in which at least one PVNGS electric generating unit operated at full power over the same period of time as the Extended Outage Period. If during the entirety of such prior time period more than one unit operated at full power, the average Effluent usage of those units shall be used to calculate the Representative Usage.

For example, on March 17, 2026, PVNGS Unit 3 shuts down and does not resume full power generation until June 20, 2026. In

addition, during this time frame, Units 2 and 3 experience short-term outages, each lasting a few weeks. Because none of the three PVNGS electric generating units operated continuously over the entire March 17 through June 20, 2026 time frame, it is necessary to consider the average Effluent usage for the electric generating units operating at full power during the entirety of the March 17, 2025 through June 20, 2025 period (or the Effluent usage of one unit if it was the only unit that operated at full power over the entirety of that period) in order to determine the Representative Usage. If such data is not available over the March 17, 2025 through June 20, 2025 period because all three units experienced an outage sometime during that period, the March 17, 2024 through June 20, 2024 period will be considered. This process will continue until the Representative Usage for at least one PVNGS unit operating at full power can be determined.

5.1.3.3. Flow Measurements during Extended Outage Period. For purposes of determining the Representative Usage pursuant to Section 5.1.3.2, above, APS shall take a totalizer reading off the Metering Devices of Effluent transferred from the PVNGS reservoirs to the circulating water canals of the PVNGS electric generating units when the Outage Unit ceases operating at full power, and a second totalizer reading when the Outage Unit resumes operating at full power. The totalizer readings taken during the year used to determine the Representative Usage shall be used as the basis for calculating the Non-Usage Fee pursuant to this Section 5.1.3.

5.1.3.4. Calculation of Non-Usage Fees in Extended Outage Period Years. In any year in which Non-Usage Fees are paid pursuant to this Section 5.1.3, the total quantity of Effluent on which such payment or payments are based shall be subtracted from the Committed Quantity in that year when determining the Non-Usage Fee payable pursuant to Section 5.1.2, above. Thus, the Non-Usage Fee payable pursuant to Section 5.2, below, shall be calculated by subtracting the Delivered Effluent Quantity in the relevant calendar year (DQ) and the total Representative Usage (RU) in that same year from the Committed Quantity in such year (CQ) and multiplying the difference by 30 percent of the Average Per Acre-Foot Price (AP) applicable in that year; or [(CQ – DQ – RU) x AP x .30].

For example, on March 17, 2026, PVNGS Unit 3 shuts down and does not resume full power generation until June 20, 2026; the Representative Usage over the Extended Outage Period for the Outage Unit was 6,500 acre-feet (AF). Assuming a Committed Quantity of 80,000 acre-feet, a Delivered Effluent Quantity of

68,500 acre-feet, and an Average Per Acre-Foot Price in 2026 of $328.50, the total Non-Usage Fees payable to Phoenix by January 31, 2027 would be calculated as follows:

Extended Outage Period: 6,500 AF x $328.50 x .20 = $427,050 (Section 5.1.3)

Non-Extended Outage Period: (80,000 AF – 68,500 AF – 6,500 AF) x $328.50 x .30 = $492,750 (Section 5.1.3.4)

Total Non-Usage Fees (2026): $427,050 + $492,750 = $919,800

5.1.3.5. Extended Outage Periods over Multiple Calendar Years: Existence Known as of December 31. In the event an Extended Outage Period extends from the calendar year for which a Non-Usage Fee is payable into the following calendar year, and the existence of that Extended Outage Period is known as of December 31 of the year for which the Non-Usage Fee is payable, the Representative Usage shall be treated as follows: The Representative Usage based on that portion of the Extended Outage Period extending from the date on which the Extended Outage Period commenced through December 31 of that same year shall be used to calculate the Non-Usage Fee payable for that year. Additionally, the Representative Usage based on that portion of any Extended Outage Period extending from January 1 of any subsequent year through the earlier of the date on which the Extended Outage Period terminates, or December 31 of that year, shall be included in the calculation of the Non-Usage Fee payable for such year.

5.1.3.6. Extended Outage Periods over Multiple Calendar Years: Existence Unknown as of December 31. In the event an Extended Outage Period extends from the calendar year for which a Non-Usage Fee is payable into the following calendar year, but the existence of that Extended Outage Period was not known as of December 31 of the year for which the Non-Usage Fee is payable and did not become known until the following year, 10 percent of that portion of the Non-Usage Fee paid for such year, which is attributable to that part of the Extended Outage Period that occurred between the date on which the Extended Outage Period commenced through December 31 of that same year (which portion of the Non-Usage Fee would have been paid pursuant to Section 5.1.2, above) shall be credited against the Non-Usage Fee payable for the following year and, to the extent the credit is not depleted, the remainder will be credited against the Non-Usage Fee payable in any subsequent years until depleted. That portion of the Non-Usage Fee for any

part of the Extended Outage Period extending from January 1 of the year immediately following the year in which the Extended Outage Period commenced shall be determined in accordance with Section 5.1.3.5, above.

5.1.3.7. Extended Outage Periods over Multiple Calendar Years: Applicable Per Acre-Foot Price. In any year in which an Extended Outage Period extends over multiple calendar years pursuant to Sections 5.1.3.5 and 5.1.3.6, above, the Average Per Acre-Foot Price used to calculate the Non-Usage Fee in accordance with this Section 5.1.3 shall be determined with reference to the Per Acre-Foot Price applicable in the calendar year in which that portion of the Extended Outage Period actually occurred.

5.2. Payment of Non-Usage Fees. By the tenth day of each January, APS shall provide to Phoenix the Representative Usage, along with the totalizer readings and calculations used to determine the Representative Usage, which totalizer readings and calculations shall be sent by facsimile or electronic mail and regular United States Mail. By the twentieth day of each January, Phoenix shall invoice APS for the Non-Usage Fee calculated pursuant to Section 5.1, above; and APS shall pay Phoenix, on behalf of the SROG Cities, the entire Non-Usage Fee by January 31 of that same year. Provided Phoenix has properly invoiced APS pursuant to this Section 5.2, if APS fails to pay the Non-Usage Fee by the due date thereof, Phoenix shall notify APS of such delinquent payment (the "Non-Usage Fee Delinquency Notice"), and APS shall pay the entire amount owed to Phoenix within 15 days after receipt of the Non-Usage Fee Delinquency Notice. If APS fails to pay the entire amount owed to Phoenix within 15 days of receipt of the Non-Usage Fee Delinquency Notice, beginning on the date on which the Non-Usage Fee was originally due, interest shall accrue on the delinquent amount at a rate of one percent per month until paid.

5.3. No Non-Usage Fee Payable upon Occurrence of Certain Events. To the extent an event that may significantly impair Phoenix's ability to comply with the SROG Cities' obligations under this Agreement (as described in Section 9.2, below) results in a decrease in the quantity of Effluent the Palo Verde Participants would have otherwise taken under this Agreement, no Non-Usage Fee shall apply to such quantity.

6. Metering Devices. Metering devices installed by APS ("Metering Devices") shall be used to measure the quantity of Effluent delivered to the Delivery Points and to measure Effluent flows for purposes of calculating the Representative Usage. Title to the Metering Devices shall be vested in the Palo Verde Participants. The Metering Devices shall be the basis for determining the Delivered Effluent Quantity. The Metering Devices shall be of a design and type acceptable to Phoenix and APS. The Palo Verde Participants shall bear the cost of the Metering Devices and the cost to install, operate, maintain, repair, replace, and calibrate the Metering Devices. APS shall calibrate the

Metering Devices no less frequently than once every six months. The SROG Cities may request in writing additional calibrations of the Metering Devices by an independent third party; *provided* that the cost incurred by the Palo Verde Participants for each additional calibration shall be reimbursed by the SROG Cities unless any such additional calibration reveals that the inaccuracy of the Metering Devices is greater than plus or minus two percent, in which case the cost of such additional calibration shall be borne by the Palo Verde Participants.

7. Effluent Quality.

7.1. Minimum Quality Standards. At all times throughout the term of this Agreement, the quality of Effluent delivered by Phoenix to the Delivery Points shall (i) be of equal or better quality as the Effluent discharged from the 91st Avenue WWTP to the Tres Rios constructed wetlands project; and (ii) meet or exceed the 91st Avenue WWTP's applicable federal and state discharge permit limits, including any amendments or replacements thereof as may be made from time to time.

7.2. Additional Effluent for Failure to Meet Minimum Quality Standards. Throughout the term of this Agreement, if, in any calendar year, the quality of Effluent delivered by Phoenix does not meet the minimum quality standards set forth in Section 7.1, above, and, as a result of such failure, cooling water usage at PVNGS is increased above 75,000 acre-feet per year based on an analysis of past blowdown rates to the PVNGS evaporation ponds, upon request by APS, Phoenix shall provide any additional Effluent required at no charge to the Palo Verde Participants up to, but not exceeding, 10 percent of the Committed Quantity for that calendar year. The additional quantity of Effluent required by this Section 7.2 shall be independent of and in addition to any additional quantities of Effluent delivered to PVNGS pursuant to Section 3.5, above. Any additional Effluent provided pursuant to this Section 7.2 shall not be a part of the Committed Quantity.

7.3. Discharge of TDS Concentrate Prohibited. The SROG Cities shall not discharge any total-dissolved-solids concentrate at any point downstream of the 91st Avenue WWTP headworks, including, without limitation, the Delivery Points. By way of example, but not limitation, the SROG Cities shall not discharge reverse osmosis concentrate streams at such points.

8. Operation and Maintenance.

8.1. SROG Cities. Phoenix shall operate, maintain, repair, and replace, at the SROG Cities' expense, the 91st Avenue WWTP as is necessary to enable the SROG Cities to carry out their obligations pursuant to Sections 3 and 7, above.

8.2. Palo Verde Participants. APS shall operate, maintain, repair, and replace, at the Palo Verde Participants' expense, all facilities, structures, and equipment owned, leased, or operated by the Palo Verde Participants, wherever located, used or useful for the receipt, treatment, storage, transportation, and use of Effluent,

including, without limitation, all such facilities, structures, and equipment that may be located on property owned by the SROG Cities or any of them ("Participants' Facilities"). Phoenix and APS may agree by separate agreement that Phoenix shall operate and maintain certain of Participants' Facilities or engage in other activities for the Palo Verde Participants and shall be compensated therefor.

9. Practices and Procedures.

9.1. APS.

9.1.1. Throughout the term of this Agreement, by June 30 of each year, APS shall provide Phoenix with a schedule setting forth the quantities of Effluent anticipated to be needed during each month of the following year.

9.1.2. Except in the event of an unplanned, unscheduled outage, APS shall give Phoenix 30 days' written notice in advance of any outage event. This notice shall include the date of the shutdown and the estimated duration of the outage.

9.1.3. If an unplanned, unscheduled outage or any other event results in a "Substantial Decrease" (defined below) in the quantity of Effluent required by PVNGS, APS shall notify Phoenix of the decreased Effluent quantity requirements as soon as reasonably practicable. "Substantial Decrease" shall mean a decrease in flow requirements of greater than 2,000 gallons per minute over a six-hour period. By way of example, but not limitation, "an unplanned, unscheduled outage or any other event" resulting in a Substantial Decrease in the quantity of Effluent required by PVNGS might include a short-notice outage of an electric generating unit, a power failure at the Hassayampa pump station, or equipment failure at the PVNGS WRF. APS shall use its best efforts to minimize the duration of any unplanned, unscheduled outage or any other events that result in a Substantial Decrease in the quantity of Effluent required by PVNGS under this Agreement. The notice required by this Section 9.1.3 shall include information detailing the reason for the decreased flow requirement and when the event giving rise to the decreased flow requirement first occurred, the expected duration of the decreased flow requirement, and on what date a return to full operating capacity is expected.

9.2. Phoenix. As soon as reasonably practicable, Phoenix shall notify APS of any event that may significantly impair Phoenix's ability to comply with the SROG Cities' obligations under this Agreement, including, without limitation, the requirements of Section 3, above, regarding quantity and the requirements of Section 7, above, regarding quality. By way of example, but not limitation, an "event that may significantly impair Phoenix's ability to comply with the SROG Cities' obligations under this Agreement" might include the loss or impairment of portions of the 91st Avenue WWTP's wastewater collection system, including,

without limitation, interceptors, or operational anomalies at the 91st Avenue WWTP that have the potential to significantly change the quantity or quality of the Effluent delivered to the Palo Verde Participants. Phoenix shall use its best efforts to minimize the duration of any events that may significantly impair Phoenix's ability to comply with the SROG Cities' obligations under this Agreement. The notice required by this Section 9.2 shall include information detailing the cause of the event that significantly impairs Phoenix's ability to comply with the SROG Cities' obligations under this Agreement and when the event first occurred, the expected duration of such event, and by what date a return to normal operations is expected.

9.3. Contact by Third Parties. The SROG Cities shall not command, authorize, direct, or instruct their agents, consultants, or contractors to contact PVNGS, including the PVNGS WRF, without the prior consent of APS.

10. New Treatment Plants. The SROG Cities shall install, operate, and maintain any new wastewater treatment plants and water reclamation plants constructed at any location other than the site of the 91st Avenue WWTP in such manner that the installation, operation, and maintenance of such new plant will not impair the ability of the SROG Cities to deliver Effluent pursuant to this Agreement.

11. PVNGS Priority. The Palo Verde Participants' right to the delivery of Effluent from the SROG Cities pursuant to this Agreement shall have priority over any other use or sale of Effluent from the 91st Avenue WWTP ("PVNGS Priority"), other than preexisting commitments to Buckeye Irrigation Company (30,000 acre-feet), the Arizona Game & Fish Department (7,300 acre-feet), the United States Water Conservation Lab (1,200 acre-feet), and each of their successors-in-interest (collectively, "Preexisting Users"), and only up to the respective quantities provided herein. Any use of the Committed Quantity by the SROG Cities or any of them and by others claiming by, through, or under the SROG Cities or any of them (other than the Preexisting Users) shall be subordinated to the rights of the Palo Verde Participants pursuant to this Agreement.

12. Location of Use. Delivered Effluent may be used by the Palo Verde Participants at PVNGS and any other electric generating facilities located within 10 miles of PVNGS. In addition, Effluent discharged from the WRSS Pipeline for purposes of maintaining and repairing the WRSS Pipeline may be used on agricultural lands adjacent to the WRSS Pipeline and/or within the service area of an irrigation or water conservation district formed pursuant to A.R.S. § 48-2901 et seq., as amended.

13. Use of Effluent. Except as required for maintenance and repair activities on the WRSS Pipeline, Effluent made available to the Palo Verde Participants pursuant to this Agreement shall not be directly or indirectly utilized other than for the purposes stated in this Agreement without prior written consent of the SROG Cities.

14. Option to Extend and True-Up Payment. In 2035, the Parties shall begin meeting to discuss a potential new agreement for the purchase and sale of Effluent or an extension of this Agreement for an additional 20 years through 2070 with no changes in PVNGS

Priority. The price terms of such new agreement or extended Agreement, which extended Agreement would be applicable for the years 2051 through 2070 only, will be negotiated at that time. If the Parties successfully negotiate a new agreement or an extension of this Agreement, and upon full execution of such new agreement or extended Agreement and approval by the governing bodies of all of the Parties, the Palo Verde Participants shall pay Phoenix, on behalf of the SROG Cities, a lump-sum true-up payment ("True-Up Payment") if the annual price adjustment cap of three percent is exceeded during the 2029 through 2035 period. The True-Up Payment shall be based on the actual rate of inflation (based on the Indices Basket) during each year that the three-percent cap was exceeded; *provided, however*, the total overall price adjustment, including the True-Up Payment, in each year of the 2029 through 2035 period shall not exceed four percent. If the Parties are unable to mutually agree on the terms of a new agreement or an extension of this Agreement, or if such new agreement or extended Agreement is not approved by all of the Parties' governing bodies, the Palo Verde Participants shall not be obligated to pay a True-Up Payment.

15. Notice of Unit Shutdown. Subject to Section 27.2, below, in the event the Palo Verde Participants intend to take out of service and permanently retire from use as a source of electric generation a PVNGS electric generating unit, the Palo Verde Participants shall provide Phoenix with at least 24 months' written notice of the date on which the unit will be shut down.

16. No Waiver of Water Rights. Nothing in this Agreement shall constitute a waiver, relinquishment, abandonment, or forfeiture of any water rights of any of the Parties.

17. Easements and Rights-of-Way. Phoenix, without cost to the Palo Verde Participants, shall grant easements, rights-of-way, leases, and licenses to the Palo Verde Participants for all Participants' Facilities as may be located at the site of the 9lst Avenue WWTP. It shall be the responsibility of Phoenix and APS to agree upon the scope and description of such easements, rights-of-way, leases, and licenses.

18. Pledge, Transfer, and Assignment of Palo Verde Participants Interest.

    18.1. The Palo Verde Participants shall have the right at any time and from time to time to mortgage, create, or provide for a security interest in or convey in trust all or part of their respective interests in this Agreement and in any property installed or maintained subject to this Agreement, including, without limitation, Participants' Facilities, to a trustee or trustees under deeds, mortgages, or indentures or to a secured party or parties under a security agreement as security for present or future successors or assigns thereof, without need for the prior written consent of any other Palo Verde Participant or the SROG Cities and without such mortgagee, trustee, or secured party assuming or becoming in any respect obligated to perform any obligations under this Agreement.

    18.2. Upon 30 days' advance written notice to the other Palo Verde Participants and the SROG Cities, any mortgagee, trustee, or secured party under present or future deeds of trust, mortgages, indentures, or security agreements of any Palo Verde

Participant and any successor or assign thereof, and any receiver, referee, or trustee in bankruptcy or reorganization of any Palo Verde Participant, and any successor by action of law or otherwise, and any purchaser, transferee, or assignee of any thereof may, without need for the prior written consent of any other Palo Verde Participant or the SROG Cities, succeed to and acquire all the rights, titles, and interests of such Palo Verde Participant in this Agreement and in any property installed or maintained subject to this Agreement and may take over possession of or foreclose upon said rights, titles, and interests of such Palo Verde Participant.

18.3. Upon 30 days' advance written notice to the SROG Cities and other Palo Verde Participants, each Palo Verde Participant shall have the right to transfer and assign all or part of its interest in this Agreement to any Person who is or will become a Palo Verde Participant without the prior written consent of the SROG Cities or any other Palo Verde Participant. Upon any such transfer, the Palo Verde Participant acquiring such interest shall assume all the duties and obligations related thereto and, with the written consent of the SROG Cities, which shall not be unreasonably withheld, the Palo Verde Participant transferring such interest shall be released and discharged therefrom.

18.4. Except as otherwise provided in Sections 18.1, 18.2, and 18.3, above, any Person succeeding to the rights, titles, and interests of a Palo Verde Participant or SROG City shall assume and agree to fully perform and discharge all of the obligations hereunder of such Palo Verde Participant or SROG City, and such Person or successor shall notify each of the other Palo Verde Participants and the SROG Cities in writing of such transfer, assignment, or merger and shall furnish to each Palo Verde Participant and the SROG Cities evidence of such transfer, assignment, or merger.

18.5. Any Palo Verde Participant or SROG City transferring or assigning any of its rights, titles, or interest in and to this Agreement shall provide 30 days' advance written notice to each of the other Palo Verde Participants and SROG Cities.

19. Improvements and Additions. The SROG Cities shall, at their sole expense, take all reasonably practical actions necessary, including, without limitation, making improvements, modifications, and additions to the 91st Avenue WWTP, to ensure compliance with the delivery quantities established in Section 3 and quality standards set forth in Section 7 hereof. If the SROG Cities fail, refuse, or are unable to make required improvements, modifications, and additions, the Palo Verde Participants shall have the right, with the concurrence of the SROG Cities, which concurrence shall not unreasonably be withheld, to install any facilities necessary to provide the treatment of Effluent required to meet such quality specifications, and payments required to be made by the Palo Verde Participants pursuant to Section 4, above, shall be reduced by the amount of all costs reasonably incurred by the Palo Verde Participants to install, operate, and maintain such facilities, including reasonable fixed charges and operation and maintenance expenses.

20. Permits and Authorizations.

20.1. Palo Verde Participants. APS shall be solely responsible for securing and maintaining in force and effect any and all permits and authorizations required by law for the transportation of Effluent from the Delivery Points to PVNGS or to any other points and for any uses of the Effluent set forth in this Agreement. APS shall use the Effluent in accordance with all applicable laws and regulations.

20.2. SROG Cities. The SROG Cities shall be solely responsible for securing and maintaining in force and effect any and all permits and authorizations required by law for the delivery of Effluent to the Palo Verde Participants at the Delivery Points and for the discharge into any watercourse or other disposal of Effluent that is not delivered to and accepted by the Palo Verde Participants pursuant to this Agreement. The SROG Cities shall deliver the Effluent to the Palo Verde Participants in accordance with all applicable laws and regulations.

20.3. Section 27.2, below, notwithstanding, if any laws or regulations governing the delivery or use of Effluent as contemplated under this Agreement are promulgated in the future so as to make it impossible or infeasible to deliver and use the Effluent as specified hereunder, the Parties shall meet to discuss in good faith how the purposes of this Agreement and intent of the Parties may be effectuated in accordance with such newly promulgated laws or regulations.

21. Destruction, Damage, or Condemnation.

21.1. If all, or any part, of the 91st Avenue WWTP is destroyed, damaged, or condemned, the SROG Cities shall restore or reconstruct the 91st Avenue WWTP in such a manner as to permit the SROG Cities to deliver Effluent to the Palo Verde Participants pursuant to this Agreement; or in the event substitute wastewater treatment facilities are constructed at a new location other than the site of the 91st Avenue WWTP, in lieu of restoration or reconstruction of the 91st Avenue WWTP, the SROG Cities shall sell and deliver the same rights to the treated wastewater from such substitute facilities on the same terms and conditions as apply to the sale and delivery of Effluent from the 91st Avenue WWTP pursuant to this Agreement. If the SROG Cities make changes to the 91st Avenue WWTP or construct substitute wastewater treatment facilities at a new location pursuant to this Section 21.1, the SROG Cities shall, at their sole expense, design, construct, and install all infrastructure necessary to deliver the Effluent pursuant to this Agreement.

21.2. If all or a portion of the Participants' Facilities are destroyed or condemned, the Palo Verde Participants shall repair, restore, or reconstruct the Participants' Facilities in a manner to permit the Palo Verde Participants to receive and transport Effluent pursuant to this Agreement.

22. Taxes.

22.1. If any general and/or special city, county, state, or other real property taxes, or any other typical taxes or imposts are properly assessed or levied against the Participants' Facilities, the Palo Verde Participants shall pay all such taxes prior to delinquency.

22.2. If any general and/or special county, state, or federal (but not city) taxes are properly assessed or levied against the purchase or use of Effluent pursuant to this Agreement, the Palo Verde Participants shall pay all such taxes prior to delinquency.

22.3. The SROG Cities or any of them shall not require the Palo Verde Participants to pay a tax resulting from the sale of Effluent by the SROG Cities or impose any assessment on the Participants' Facilities. If, contrary to this Section 22.3, the SROG Cities or any of them imposes an assessment or levies a tax on the Participants' Facilities that has the effect of raising the price of Effluent under this Agreement, the price of Effluent shall be decreased by the amount of such tax or assessment.

22.4. If any general and/or special city, county, state, or other real property taxes, or any other type of taxes or imposts are assessed or levied against the 91st Ave WWTP, the SROG Cities shall pay all such taxes prior to delinquency.

22.5. Nothing contained in this Section 22 shall be construed as a recognition or admission by the SROG Cities or the Palo Verde Participants of the validity of any particular tax or assessment.

23. Liability, Indemnification, and Insurance.

23.1. Liability of SROG Cities. Except for the negligence or willful misconduct of the Palo Verde Participants, their officers, directors, employees, and agents, the SROG Cities shall be liable insofar as the Palo Verde Participants are concerned for any physical damage to property and death of, and personal injury to, anyone arising out of the ownership, use, occupancy, operation, maintenance, repair, replacement, and reconstruction of the 9lst Avenue WWTP; and the SROG Cities hereby indemnify and hold the Palo Verde Participants harmless for, from, and against any cost, expense, claim, or loss from such damage or injury.

23.2. Liability of Palo Verde Participants. Except for the negligence or willful misconduct of the SROG Cities, their officers, councilmembers, managers, employees, or agents, the Palo Verde Participants shall be liable insofar as the SROG Cities are concerned for any physical damage to property and death of, and personal injury to, anyone arising out of the Palo Verde Participants' ownership, use, occupancy, operation, maintenance, repair, replacement, and reconstruction of the Participants' Facilities; and the Palo Verde Participants hereby indemnify

and hold the SROG Cities harmless for, from, and against any cost, expense, claim, or loss from such damage or injury.

23.3. Indemnification for Use of Delivered Effluent. The Palo Verde Participants shall indemnify the SROG Cities for, from, and against any claim resulting from the control, transmission, use, or disposal of Effluent by the Palo Verde Participants after delivery thereof by the SROG Cities to the Delivery Points, except to the extent such claim is the result of the SROG Cities' failure to comply with the quality standards set forth in Section 7.1, above.

23.4. Insurance. The SROG Cities and the Palo Verde Participants shall procure and maintain insurance against physical damage to property and death of, and personal injury to, persons of the kind and with coverages normally carried by entities operating properties similar to the 91st Avenue WWTP and the Participants' Facilities. Nothing contained in this Section 23.4 shall prohibit the SROG Cities and the Palo Verde Participants from adopting a self-insurance program of a type and kind being utilized by entities operating properties similar to the 91st Avenue WWTP and the Participants' Facilities. Upon request, the SROG Cities and the Palo Verde Participants shall furnish the others with certifications of insurance demonstrating compliance with this Section 23.4.

24. Cooperation of the Parties.

24.1. Each of the SROG Cities and the Palo Verde Participants shall fully cooperate with and assist one another in securing and maintaining in force any and all licenses, permits, authorizations, approvals, and consents required in accordance with this Agreement or by local, state, or federal laws and regulations and shall render such assistance to the other Parties as it or they may reasonably request.

24.2. Each of the SROG Cities and the Palo Verde Participants shall fully cooperate with and assist one another in any and all judicial and administrative proceedings required in or related to the performance of this Agreement.

24.3. Each of the SROG Cities and the Palo Verde Participants shall make, execute, and deliver all documents and instruments necessary or useful to the implementation and performance of this Agreement.

24.4. In the event any proceeding at law or equity is instituted involving the authority and power of any of the SROG Cities and/or the Palo Verde Participants to make, execute, and deliver this Agreement and/or to perform its terms, covenants, and conditions, or is relating to the rights, title, and interest of any of the SROG Cities or the Palo Verde Participants in and to Effluent, then the SROG Cities and the Palo Verde Participants shall jointly and cooperatively defend the validity of this Agreement and the use of Effluent intended hereunder.

25. Interruption of Delivery of Effluent.

25.1. Subject to Section 25.2 below, the SROG Cities shall have the right to refuse to deliver Effluent under the terms of this Agreement when all of the following have occurred: (i) there exists in the SROG Cities a critical need for water to be used for domestic purposes; (ii) subject to Section 11, above, all other reasonable sources of water in excess of the Committed Quantity have been exhausted; (iii) reasonable steps have been taken by the SROG Cities to conserve their municipal water supplies; and (iv) the SROG Cities have given the Palo Verde Participants reasonable notice of the critical need in accordance with the requirements of Section 28.3, below. When the critical need expires, or when other reasonable sources of water become available, the SROG Cities may no longer refuse to deliver Effluent pursuant to this Agreement. The SROG Cities shall use their best efforts to resume deliveries of Effluent pursuant to this Agreement at the earliest practicable time if such deliveries are interrupted pursuant to this Section 25.

25.2. Prior to designating the existence of a critical need and temporarily discontinuing Effluent deliveries to the Palo Verde Participants pursuant to Section 25.1, above, the SROG Cities shall consider the critical need for energy to support the Parties' respective customer bases by expressly acknowledging the symbiotic relationship between water and energy in the desert state of Arizona and the interdependency of these two vital resources by taking into account the mutual critical need each Party has for the other's product.

26. Dispute Resolution; Default and Termination.

26.1. In the event of a dispute arising out of or relating to this Agreement, the Parties shall attempt in good faith to resolve such dispute promptly by negotiation between representatives having authority to settle the controversy. All reasonable requests for information made by one Party to the other shall be honored.

26.2. The Parties shall pay all monies and carry out all other performances, duties, and obligations agreed to be paid and/or performed by them pursuant to the terms and conditions set forth and contained in this Agreement. A default by a Party in its covenants and obligations shall be an act of default under this Agreement ("Default").

26.3. In the event of a Default by a Party, within 30 days following the giving of written notice of such Default by the non-defaulting Party, the defaulting Party shall remedy such Default either by advancing the necessary funds and/or rendering the necessary performance, as the context so requires. The notice required by this Section 26.3 shall clearly identify the specific nature of the Default and the steps required to cure the same.

26.4. In the event that a Party disputes an asserted Default, such Party shall pay the disputed payment or perform the disputed obligation, but may do so under protest, which protest shall be in writing, shall accompany the disputed payment or

precede the performance of the disputed obligation, and shall specify the reasons upon which the protest is based. Payments not made under protest shall be deemed to be correct.

26.5. In the event of a Default by a Party in the payment or performance of any obligation under this Agreement, which continues for a period of 60 days or more without having been cured by the defaulting Party, or without the defaulting Party having commenced or continued action in good faith to cure such Default, then, at any time thereafter and while said Default is continuing, the non-defaulting Party at its option may, by written notice to the defaulting Party, terminate this Agreement.

26.6. If this Agreement is terminated for any reason, Phoenix shall have the immediate right of re-entry of any easement or leasehold granted to the Palo Verde Participants pursuant to Section 17, above. APS shall, as soon as reasonably practicable or within such other time frame as the Parties may agree, remove all facilities owned by the Palo Verde Participants located on property owned by the SROG Cities or any of them. All facilities not removed from such property within such time frame shall become the property of the owner of such real property.

27. Performance and Uncontrollable Circumstance.

27.1. Performance. All terms, covenants, and conditions to be performed by the Parties under this Agreement shall be performed at the sole expense of the Party so obligated, and if another Party pays any sum of money or does any act that requires the payment of money, by reason of the failure, neglect, or refusal of the obligated Party to perform such term, covenant, or condition, the sum of money so paid by the other Party shall immediately be payable to the non-obligated Party by the Party obligated to perform.

27.2. Uncontrollable Circumstance. A Party shall not be considered to be in Default in the performance of any of the obligations under this Agreement (other than obligations of a Party to pay costs and expenses) if failure of performance is due to an Uncontrollable Circumstance. The term “Uncontrollable Circumstance” means any act, event, or condition that is caused by or due to circumstances beyond the reasonable control of the Party relying thereon as justification for not performing an obligation or complying with any condition required of such Party under this Agreement and that materially interferes with such Party’s obligations under this Agreement (other than payment obligations) to the extent that such act, event, or condition is not the result of the willful or negligent act, error or omission, failure to exercise reasonable diligence, or breach of this Agreement on the part of such Party. By way of example, but not limitation, each of the following shall constitute an Uncontrollable Circumstance: failure of facilities, flood, earthquake, tornado, storm, fire, lightning, epidemic, war, riot, civil disturbance or disobedience, labor dispute, action or non-action by or failure to obtain the necessary authorizations or approvals from any governmental agency

or authority or the electorate, labor or material shortage, sabotage, restraint by court order, law, regulation, or public authority, and the forced shutdown of PVNGS or the 91st Avenue WWTP by a governmental body, which by exercise of due diligence and foresight such Party could not reasonably have been expected to avoid and which, by exercise of due diligence it is unable to overcome. Nothing contained in this Section 28.2 shall be construed so as to require a Party to settle any strike or labor dispute in which it may be involved. A Party rendered unable to fulfill any obligation by reason of an Uncontrollable Circumstance shall, as soon as reasonably practicable, notify the others of the event giving rise to such Uncontrollable Circumstance, and exercise due diligence to remove such inability with all reasonable dispatch.

28. General Provisions.

28.1. Incorporation of Recitals and Exhibit. The Recitals set forth in Paragraphs A through K, above, and Exhibit "A" attached to this Agreement (but not the attached Appendix) are incorporated here by this reference as if fully set forth in this Agreement, and are acknowledged and agreed to by the Parties.

28.2. Case; Section Headings. The use of the singular or plural number shall be deemed to include the other uses whenever the context so requires. The section headings used in this Agreement are for convenience and reference only and do not define, limit, or describe the scope or intent of any provision of this Agreement.

28.3. Notices. Notices shall be in writing and shall be given by: (a) personal delivery; (b) national overnight delivery service; or (c) United States Mail, certified mail, return receipt requested, postage prepaid. Notices shall be delivered or addressed to the addresses set forth below or at such other address as APS or Phoenix may designate in writing. The date a notice shall be deemed to have been given, received, and become effective shall be: (i) the date on which the notice is delivered or refused, if notice is given by personal delivery or delivery by a national overnight delivery service; or (ii) three days following the date of deposit in the mail, if the notice is sent by certified United States Mail, return receipt requested and postage prepaid. No notice shall be deemed effective unless sent in one of the manners described above.

To Phoenix:
Director of Water Services
City of Phoenix
200 West Washington Street
Phoenix, Arizona 85003

To PVNGS:
Palo Verde Nuclear Generating Station
Att'n: Water Reclamation Facility Manager
5801 South Wintersburg Road, M.S. 6215
Tonopah, Arizona 85354-7529

with a copy to APS: Arizona Public Service Company
Att'n: Water Resources Manager
P.O. Box 52034, M.S. 9724
Phoenix, Arizona 85072-2034

Any Party referenced in this Section 28.3 may change the address or addressee to which notices are to be sent by giving notice of such change of address or addressee in conformity with the provisions of this Section 28.3.

28.4. Remedies Cumulative. The remedies provided for in this Agreement shall be cumulative. All remedies available under this Agreement shall be in addition to any and all remedies at law or in equity.

28.5. Successors and Assigns. The terms, covenants, and conditions of this Agreement shall be binding upon, and inure to the benefit of and shall apply to the respective transferees, successors, and assigns of the transferring Party.

28.6. Governing Law. This Agreement shall be governed by, and construed in accordance with, the laws of the State of Arizona.

28.7. Entire Agreement. The Parties expressly acknowledge that they have read this Agreement and understand all of its terms, covenants, and conditions, and that this Agreement constitutes the entire agreement with respect to any matters referred to in this Agreement. This Agreement supersedes any and all other understandings, agreements, correspondence, or communications between the Parties with respect to the matters embodied in this Agreement, including Agreement No. 13904, which shall be of no further force and effect.

28.8. Modification. No changes, alterations, or modifications to this Agreement shall be effective unless in writing and signed by an authorized representative of each of the Parties.

28.9. Waiver. The failure of a Party to insist, in any one or more instances, on performance of any of the terms, covenants, or conditions of this Agreement shall not be construed as a waiver or relinquishment of any rights granted under this Agreement or of the future performance of any such term, covenant, or condition, and the obligations of the Parties with respect thereto shall continue in full force and effect. No waiver of any provision or condition of this Agreement by a Party shall be valid unless in writing signed by such Party. A waiver by one Party of the performance of any covenant or condition of another Party shall not invalidate this Agreement, nor shall such waiver be construed as a waiver of any other covenant or condition.

28.10. No Party the Drafter. This Agreement is the product of negotiation between the Parties, and no Party is deemed the drafter of this Agreement.

28.11. Conflict of Interest. The provisions of A.R.S. § 38-511 are incorporated in this Agreement to the extent of their applicability to contracts of the nature of this Agreement under the laws of the State of Arizona.

28.12. Counterpart Execution. This Agreement may be signed in counterparts, each of which shall be an original and all of which shall constitute one and the same instrument. All signatures need not be on the same counterpart.

28.13. Authorizations. The signatories to this Agreement represent that they have been appropriately authorized to enter into this Agreement on behalf of the Party for which they sign and that no further action or approvals are necessary before execution of this Agreement.

IN WITNESS WHEREOF, the Parties have executed this Agreement as of _____ _____, 2010.

[Remainder of page intentionally left blank]

CITY OF PHOENIX,
an Arizona municipal corporation

By: /s/ David Cavazos
Its: City Manager

Attest:

/s/ Mario Paniagua
City Clerk

Approved as to Form:

/s/ Gary Verburg
Acting Phoenix City Attorney

STATE OF ARIZONA)
)ss.
County of Maricopa)

On April, 14 2010, before me, Dawnell M. Navarro, a Notary Public in and for the State of Arizona, personally appeared David Cavazos, personally known to me (or proved to me on the basis of satisfactory evidence) to be the City Manager and _____ of the CITY OF PHOENIX, an Arizona municipal corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such _____ and _____.

WITNESS my hand and official seal.

/s/ Dawnell M. Navarro
Notary Public

My Commission Expires:

March 30, 2013

Dawnell M. Navarro
NOTARY PUBLIC -- ARIZONA
MARICOPA COUNTY
My Commission Expires
March 30, 2013

CITY OF MESA,
an Arizona municipal corporation

By: /s/ Christopher J. Brady
Its: City Manager

Attest:

/s/ Linda Crocker
City Clerk

Approved as to Form:

/s/ Wilbert J. Taebel
Mesa City Attorney

STATE OF ARIZONA)
)ss.
County of Maricopa)

On April, 29 2010, before me, Ann Webster, a Notary Public in and for the State of Arizona, personally appeared Christopher J. Brady, personally known to me (or proved to me on the basis of satisfactory evidence) to be the City Manager and _____ of the CITY OF MESA, an Arizona municipal corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such City Manager and _____.

WITNESS my hand and official seal.

/s/ Ann Webster
Notary Public

My Commission Expires:

May 27, 2010

CITY OF TEMPE,
an Arizona municipal corporation

By: /s/ Hugh Hallman
Its: Mayor

Attest:

/s/ Jan Hort
City Clerk

Approved as to Form:

/s/ Andrew B. Ching
Tempe City Attorney

STATE OF ARIZONA)
)ss.
County of Maricopa)

On April 26, 2010, before me, Kay Savard, a Notary Public in and for the State of Arizona, personally appeared Hugh Hallman & Jan Hort, personally known to me (or proved to me on the basis of satisfactory evidence) to be the Mayor and City Clerk of the CITY OF TEMPE, an Arizona municipal corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such _____ and _____.

WITNESS my hand and official seal.

/s/ Kay E. Savard
Notary Public

My Commission Expires:

Aug. 20, 2013

CITY OF SCOTTSDALE,
an Arizona municipal corporation

By: /s/ W. J. Lane
Its: Mayor

Attest:

/s/ Carolyn Jagger
City Clerk

Approved as to Form:

/s/ Steven B. Bennett
Scottsdale City Attorney

STATE OF ARIZONA)
)ss.
County of Maricopa)

On April, 19 2010, before me, K. Stevens, a Notary Public in and for the State of Arizona, personally appeared Jim Lane and Carolyn Jagger, personally known to me (or proved to me on the basis of satisfactory evidence) to be the Mayor and City Clerk of the CITY OF SCOTTSDALE, an Arizona municipal corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such Mayor and City Clerk.

WITNESS my hand and official seal.

/s/ K. Stevens
Notary Public

My Commission Expires:

Nov. 28, 2013

CITY OF GLENDALE,
an Arizona municipal corporation

By: /a/ Pamela J. Kavanaugh
Its: Assistant City Manager

Attest:

/s/ Pamela Hanna
City Clerk

Approved as to Form:

/s/ Craig D. Tindall
Glendale City Attorney

STATE OF ARIZONA)
)ss.
County of Maricopa)

On April, 16 2010, before me, Summer Steinke, a Notary Public in and for the State of Arizona, personally appeared Pam Kavanaugh, personally known to me (or proved to me on the basis of satisfactory evidence) to be the Assistant City Manager of the CITY OF GLENDALE, an Arizona municipal corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such Assistant City Manager.

WITNESS my hand and official seal.

/s/ Summer Steinke
Notary Public

My Commission Expires:

1/9/2011

ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation

By: /s/ Randall K. Edington
Its: EVP & CNO

Attest:

/s/ Diane Wood

STATE OF ARIZONA)
)ss.
County of Maricopa)

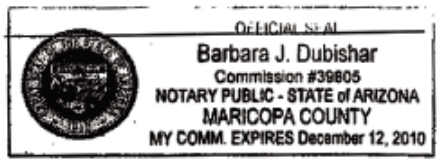
On April, 23 2010, before me, Barbara J. Dubishar, a Notary Public in and for the State of Arizona, personally appeared Randall K. Edington AND Diane Wood, personally known to me (or proved to me on the basis of satisfactory evidence) to be the EVP & CNO and Associate Secretary of ARIZONA PUBLIC SERVICE COMPANY, an Arizona corporation, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the ~~municipal~~ (BJD) corporation by themselves and as such EVP & CNO and Associate Secretary.

WITNESS my hand and official seal.

/s/ Barbara J. Dubishar
Notary Public

My Commission Expires:

December 12, 2010



SALT RIVER PROJECT AGRICULTURAL
IMPROVEMENT AND POWER DISTRICT, an
Arizona municipal corporation
and agricultural improvement district

By: /s/ John M. Williams, Jr.
Its: President

Attest and Countersign:

/s/ Terrill A. Lonon

Approved as to Form:

/s/ Frederic L. Beeson

STATE OF ARIZONA)
)ss.
County of Maricopa)

On March, 26, 2010, before me, Fay A. Wehofer, a Notary Public in and for the State of Arizona, personally appeared John M. Williams Jr, and Terrill A. Lonon, personally known to me (or proved to me on the basis of satisfactory evidence) to be the President and Secretary of the SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT, an Arizona municipal corporation and agricultural improvement district, and that they being authorized to do so, executed the foregoing instrument for the purposes therein contained by signing the name of the municipal corporation by themselves and as such President and Secretary.

WITNESS my hand and official seal.

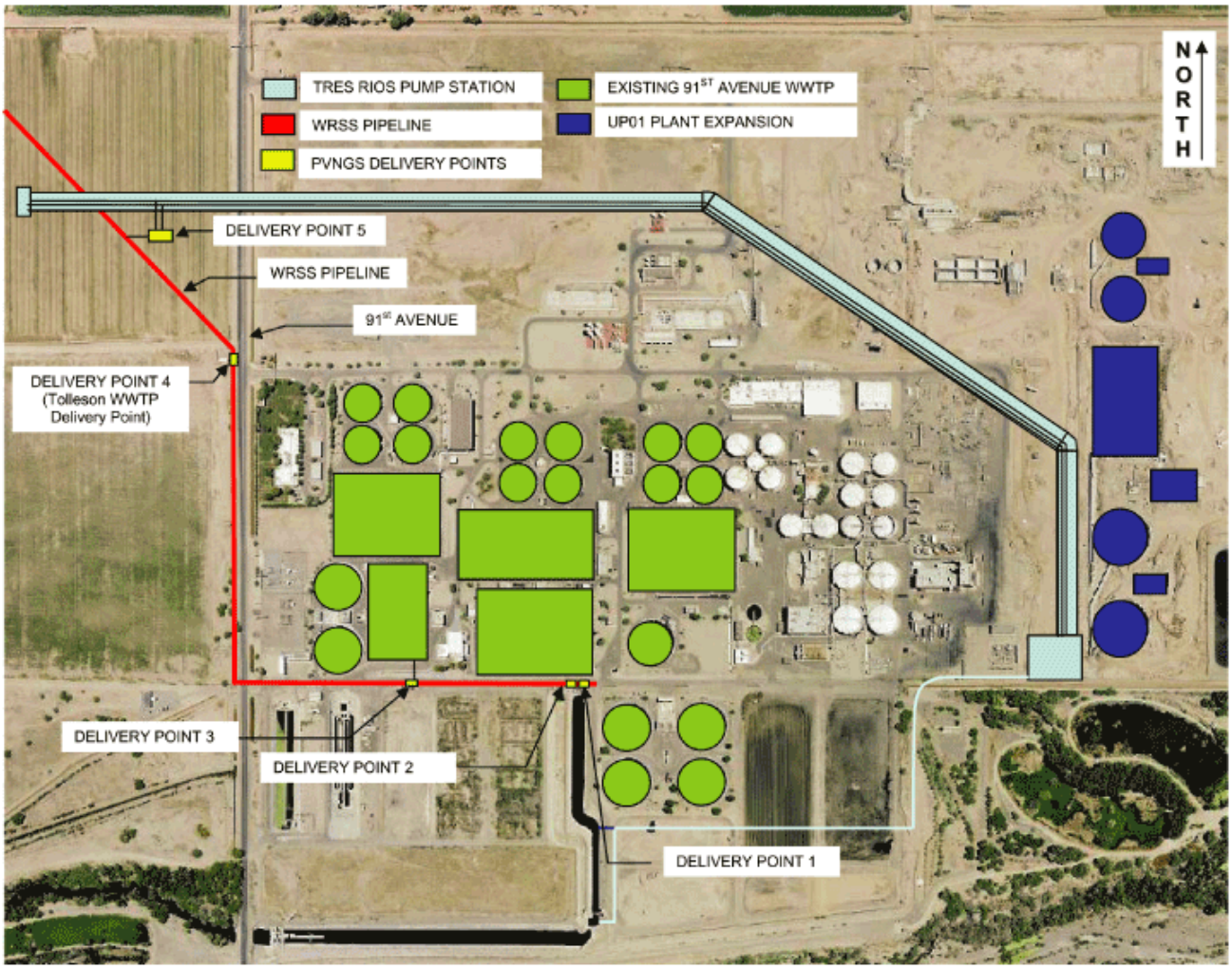
/s/ Fay A. Wehofer
Notary Public

My Commission Expires:

11/27/2011

EXHIBIT "A"

MAP OF DELIVERY POINTS



APPENDIX†

EXAMPLES OF NON-USAGE FEE CALCULATIONS UNDER MUNICIPAL EFFLUENT PURCHASE AND SALE AGREEMENT

For purposes of this Appendix, a Committed Quantity of 80,000 acre-feet (AF) is assumed. In addition, this Appendix assumes the following for the years 2028 and 2029:

2028

Delivered Effluent Quantity: 65,000 AF
Per Acre-Foot Price:
- Tier 1 — $198.00
- Tier 2 — $293.00
- Tier 3 — $349.00
- Tier 4 — $474.00

Average Per-Acre-Foot Price: $328.50 [($198.00 + $293.00 + $349.00 + $474.00) ÷ 4]

Outage Periods and Effluent Usage

Unit 1 outage: May 1 through August 31 = 123 days
- Unit 2 Effluent usage from May 1 through August 31: 8,220 AF
- Unit 3 Effluent usage from May 1 through August 31: 8,230 AF

Unit 3 outage: November 16 through December 31 = 45 days (outage ongoing into 2029)
- Unit 1 Effluent usage from November 16 through December 31: 2,318 AF
- Unit 2 Effluent usage from November 16 through December 31: 2,316 AF

2029

Delivered Effluent Quantity: 72,500 AF
Per Acre-Foot Price:
- Tier 1 — $203.94
- Tier 2 — $301.79
- Tier 3 — $359.47
- Tier 4 — $488.22

Average Per-Acre-Foot Price: $338.36 [(203.94 + 301.79 + 359.47 + 488.22) ÷ 4]

Outage Period and Effluent Usage

Unit 3 outage: January 1 through February 28 = 59 days (outage continuing from 2028)
- Unit 1 Effluent usage from January 1 through February 28: 3,040 AF
- Unit 2 Effluent usage from January 1 through February 28: 3,036 AF

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† This Appendix is for illustrative purposes only and is neither incorporated into nor made a part of the Municipal Effluent Purchase and Sale Agreement. Capitalized terms used in this Appendix shall have the meanings ascribed to them in the Municipal Effluent Purchase and Sale Agreement.

In 2028, the Unit 1 outage lasted for a total of 123 days. Therefore, pursuant to Section 5.1.3.1, it is an Extended Outage Period. Based on the totalizer readings taken pursuant to Section 5.1.3.3, pursuant to Section 5.1.3.2, the Representative Usage for the Unit 1 Extended Outage Period would be calculated by taking the average Effluent usage of the two remaining PVNGS electric generating units operating at full power (*i.e.*, Units 2 and 3) over that same period, or 8,225 AF [(8,220 AF + 8,230 AF) ÷ 2]. In 2028, Unit 3 was also in an outage that commenced on November 16 and continued through the end of that year. However, because only 45 days had passed, the outage was not treated as an Extended Outage Period and, as a result, the Palo Verde Participants paid the higher 30 percent Non-Usage Fee on that portion of the outage extending from November 16 through December 31.

Pursuant to Sections 5.1.3.4 and 5.2, by January 31, 2029, the Palo Verde Participants would pay Phoenix, on behalf of the SROG Cities, a Non-Usage Fee of $1,208,058.75 calculated as follows:

Portion of 2028 Non-Usage Fee Payable over Extended Outage Period

$540,382.50 [8,225 AF x $328.50 x .20]

Portion of 2028 Non-Usage Fee Payable over Non-Extended Outage Period

$667,676.25 [(80,000 AF – 65,000 AF – 8,225 AF) x $328.50 x .30]

Total 2028 Non-Usage Fee: $540,382.50 + $667,676.25 = $1,208,058.75

In 2029, there was only one outage—an outage to Unit 3, which was a continuation of the outage that commenced on November 16, 2028. Because the outage lasted 104 days until Unit 3 resumed full power on February 28, 2029, it constituted an Extended Outage Period. The Representative Usage for that portion of the Unit 3 Extended Outage Period occurring from January 1, 2029 through February 28, 2029 would be calculated by taking the average Effluent usage of the two remaining PVNGS electric generating units operating at full power (*i.e.*, Units 1 and 2) over that same period, or 3,038 AF [(3,040 AF + 3,036 AF) ÷ 2].

Because that portion of the Unit 3 outage extending from November 16 through December 31, 2028 was not treated as an Extended Outage Period (because the existence of such Extended Outage Period was unknown as of December 31 of that year), the Palo Verde Participants paid the higher 30 percent Non-Usage Fee for that 45-day period. Therefore, pursuant to Section 5.1.3.6, 10 percent of that portion of the Non-Usage Fee attributable to that part of the Extended Outage Period extending from November 16 through December 31, 2028 must be credited against the Non-Usage Fee payable in 2029. To determine the amount of the credit, the Representative Usage for that portion of the Unit 3 Extended Outage Period occurring from November 16, 2028 through December 31, 2028 must be calculated by taking the average Effluent usage of the two remaining PVNGS electric generating units operating at full power (*i.e.*, Units 1 and 2) over that same period, or 2,317 AF [(2,318 AF + 2,316 AF) ÷ 2].

By January 31, 2030, the Palo Verde Participants would pay Phoenix, on behalf of the SROG Cities, a Non-Usage Fee of $582,402.79 calculated as follows:

Portion of 2029 Non-Usage Fee Payable over Extended Outage Period

$205,587.54 [3,038 AF x $338.36 x .20]

Portion of 2029 Non-Usage Fee Payable over Non-Extended Outage Period

$452,928.70 [(80,000 AF – 72,500 AF – 3,038 AF) x $338.36 x .30]

Credit for that Portion of Extended Outage Period Occurring in 2028

$76,113.45 [2,317 AF x $328.50 x .10]

Total 2029 Non-Usage Fee: $205,587.54 + $452,928.70 – $76,113.45 = $582,402.79

Exhibit 10.2

REIMBURSEMENT AGREEMENT

among

ARIZONA PUBLIC SERVICE COMPANY

THE BANKS PARTY HERETO

and

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent and Issuing Bank

dated as of April 16, 2010

J.P. Morgan Securities Inc. and Union Bank, N.A.,
Joint Lead Arrangers and Joint Bookrunners

TABLE OF CONTENTS

The Table of Contents is not a part of this Agreement.

REIMBURSEMENT AGREEMENT

REIMBURSEMENT AGREEMENT among ARIZONA PUBLIC SERVICE COMPANY, JPMORGAN CHASE BANK, N.A., as Administrative Agent and as Issuing Bank, and the BANKS listed on the signature pages hereto, dated as of April 16, 2010. (Unless otherwise indicated, all capitalized terms used herein have the meanings referred to or set forth in Section 1.)

WHEREAS, the Company has entered into a Participation Agreement dated as of August 1, 1986 (as amended and in effect on April 16, 2010, the "**Participation Agreement**") among the Company, U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston), for itself and as Owner Trustee (together with its successors in such capacity, the "**Owner Trustee**"), The Bank of New York Mellon (as successor to JPMorgan, as successor to Chemical Bank), for itself and as Indenture Trustee (together with its successors in such capacity, the "**Indenture Trustee**"), PVNGS Funding Corp., Inc., PVNGS II Funding Corp., Inc. and Security Pacific Capital Leasing Corporation, as Equity Participant (together with its successors and assigns, the "**Equity Participant**"), relating to the acquisition of an undivided interest in PVNGS Unit 2 through a trust for the benefit of the Equity Participant which interest has been leased to the Company pursuant to a lease dated as of August 1, 1986 between the Owner Trustee and the Company (as amended and in effect on April 16, 2010, the "**Facility Lease**");

WHEREAS, pursuant to Section 10(b)(3)(ix) of the Participation Agreement, the Company has agreed to maintain at all times during the Basic Lease Term (as defined in the Participation Agreement) an irrevocable letter of credit for the benefit of the Equity Participant;

WHEREAS, in order to comply with the requirements of Section 10(b)(3)(ix) of the Participation Agreement, the Company entered into a Reimbursement Agreement dated as of August 1, 1986 (as amended and restated thereafter from time to time prior to July 22, 2002, further amended and restated as of July 22, 2002, as further amended and restated as of May 19, 2005, and in effect immediately prior to April 16, 2010, the "**Existing Reimbursement Agreement**") between the Company and JPMorgan, pursuant to which JPMorgan issued to the Equity Participant its irrevocable transferable letter of credit (such letter of credit, as amended and restated and in effect from time to time before May 19, 2005, as further amended and restated as of May 19, 2005, as further amended and restated as of April 16, 2010, and as the same may be amended in accordance with this Agreement and in effect from time to time hereafter, and any successor Letter of Credit as provided in such Letter of Credit, being referred to herein as the "**Letter of Credit**"), to secure the payment of Rent (as defined in the Participation Agreement) by the Company under the Facility Lease to the extent of the amount available to be drawn from time to time under the Letter of Credit;

WHEREAS, the Letter of Credit will expire on May 19, 2010, if not extended; and

WHEREAS, the Company has requested that the Letter of Credit be deemed to be issued pursuant to this Agreement as of the date hereof and immediately amended and restated in substantially the form of Exhibit A hereto to provide, inter alia, that the term of the Letter of

Credit be extended for three years, and the Banks are willing to comply with such requests on the terms and conditions set forth below;

NOW, THEREFORE, in consideration of the premises and in order to induce the Banks to agree to deem the Letter of Credit to be issued pursuant to this Agreement and to amend and restate the Letter of Credit, including to extend the term of the Letter of Credit, the parties hereto agree, upon satisfaction of the conditions set forth in Section 3(b) below and subject to Section 3(c) below, as follows:

Section 1. *Definitions; Accounting Terms*. (a) Definitions. Capitalized terms used herein and not otherwise defined herein have the respective meanings assigned thereto in Appendix A to the Facility Lease. The following terms as used herein have the following respective meanings:

"**ACC**" means the Arizona Corporation Commission or any successor thereto.

"**Administrative Agent**" means JPMorgan, in its capacity as administrative agent for the Banks hereunder, and its successors in such capacity.

"**Administrative Questionnaire**" means, with respect to each Bank, an administrative questionnaire in the form prepared by the Administrative Agent and submitted to the Administrative Agent (with a copy to the Company) duly completed by such Bank.

"**Affiliate**" means, as to any Person, any other Person that, directly or indirectly, controls, is controlled by or is under common control with such Person or is a director or officer of such Person.

"**Agent Parties**" has the meaning given in Section 11(d).

"**Agreement**" means, when used with reference to this Agreement, this Reimbursement Agreement, as the same may be amended in accordance with its terms from time to time.

"**Amended and Restated Letter of Credit**" means the Amended and Restated Irrevocable Transferable Letter of Credit No. P-010151 (formerly numbered as S-1001), dated as of April 16, 2010, amending the Existing Letter of Credit, substantially in the form of Exhibit A hereto.

"**Applicable Booking Office**" means, as to each Bank, its office, branch or affiliate located at its address set forth in its Administrative Questionnaire (or identified in its Administrative Questionnaire as its Applicable Booking Office) or such other office, branch or affiliate of such Bank as it may hereafter designate as its Applicable Booking Office by notice to the Company and the Administrative Agent.

"**Assignee**" has the meaning set forth in Section 15(a).

"**Assignment and Assumption**" means an assignment and assumption entered into by a Bank and an Assignee (with the consent of any party whose consent is required by Section 15), and accepted by the Administrative Agent, substantially in the form of Exhibit B attached hereto.

"**Authorized Officer**" means the chairman of the board, chief executive officer, president, chief financial officer, chief operating officer, chief accounting officer, treasurer, controller, any vice president or any assistant treasurer of the Company.

"**Bank**" means (i) each bank or financial institution listed on the signature pages hereof, each Assignee that becomes a Bank pursuant to Section 15(a), and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"**Base Rate**" means, for any day, a rate per annum equal to the greatest of (a) the Prime Rate in effect on such day, (b) the Federal Funds Rate in effect on such day plus ½ of 1% and (c) the LIBO Rate for a one month interest period on such day (or if such day is not a Business Day, the immediately preceding Business Day) plus 1%. Any change in the Base Rate due to a change in the Prime Rate, the Federal Funds Rate or the LIBO Rate shall be effective from and including the effective date of such change in the Prime Rate, the Federal Funds Rate or the LIBO Rate, respectively.

"**Base Rate Margin**" means a rate per annum determined in accordance with Schedule I hereto.

"**Business Day**" means any day except (i) a Saturday or Sunday, (ii) any other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California or, for purposes of Sections 2(a), 2(g) and 9(i) only, Phoenix, Arizona, are authorized by law to close, or (iii) a day on which payments in respect of the Letter of Credit cannot be funded via wire through the Federal Reserve System.

"**Capital Lease Obligations**" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are required to be classified and accounted for as a capital lease on the balance sheet of such Person under GAAP and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with GAAP.

"**Code**" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"**Company**" means Arizona Public Service Company, an Arizona corporation, and its successors and permitted assigns.

"**Company Materials**" has the meaning given in Section 7(g).

"**Consolidated**" has the meaning set forth in Section 8(e).

"**Consolidated Capitalization**" has the meaning set forth in Section 8(e).

"**Consolidated Indebtedness**" has the meaning set forth in Section 8(e).

"**Consolidated Net Worth**" has the meaning set forth in Section 8(e).

"**Consolidated Subsidiary**" means at any date any Subsidiary or other entity the accounts of which would be consolidated with those of the Company in its consolidated financial statements if such statements were prepared as of such date.

"**Date of Early Termination**" has the meaning set forth in the Letter of Credit.

"**Debtor Relief Laws**" means the Bankruptcy Code of the United States, and all other liquidation, conservatorship, bankruptcy, assignment for the benefit of creditors, moratorium, rearrangement, receivership, insolvency, reorganization, or similar debtor relief laws of the United States or other applicable jurisdictions from time to time in effect and affecting the rights of creditors generally.

"**Defaulting Bank**" means any Bank, as reasonably determined by the Administrative Agent or if the Administrative Agent is the Defaulting Bank, by the Required Banks, that (a) has defaulted in its obligation to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement, (b) has notified the Company, the Administrative Agent, the Issuing Bank or any Bank in writing of its intention not to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement, (c) has otherwise failed to pay over to the Administrative Agent or any other Bank any other amount required to be paid by it hereunder within three (3) Business Days of the date when due, (d) has failed, within three (3) Business Days after request by the Administrative Agent, or if the Administrative Agent is the Defaulting Bank, by the Required Banks, to confirm that it will comply with the terms of this Agreement relating to its obligations to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement or (e) shall (or whose parent company shall) generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or shall have had any proceeding instituted by or against such Bank (or its parent company) seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for, it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 30 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for it or for any substantial part of its property) shall occur, or shall take (or whose parent company shall take) any corporate action to authorize any of the actions set forth above in this clause (e); provided that a Bank shall not be deemed to be a Defaulting Bank solely by virtue of the ownership or assumption of any equity interest in any Bank or any Person that directly or indirectly controls such Bank by a governmental authority or an instrumentality thereof.

"**Disbursement Advance**" has the meaning set forth in Section 2(a).

"**Effective Date**" has the meaning set forth in Section 3(b).

"**Eligible Institution**" means (i) a commercial bank or a savings and loan association having a net worth in excess of $250,000,000 (or the equivalent in any other currency), (ii) a Bank or an affiliate of a Bank or (iii) any other Person which the Company designates as an Eligible Institution with the consent of the Administrative Agent.

"**Equity Participant**" has the meaning set forth in the first recital hereto.

"**ERISA**" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"**ERISA Affiliate**" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"**Existing Letter of Credit**" means the Letter of Credit, as amended and in effect immediately prior to April 16, 2010.

"**Existing Reimbursement Agreement**" has the meaning set forth in the third recital hereto.

"**Facility Lease**" has the meaning set forth in the first recital hereto.

"**Federal Funds Rate**" means, for any day, the rate per annum (rounded upward, if necessary, to the nearest 1/100th of 1%) equal to the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day, *provided* that (i) if such day is not a Business Day, the Federal Funds Rate for such day shall be such rate on such transactions on the next preceding Business Day as so published on the next succeeding Business Day, and (ii) if no such rate is so published on such next succeeding Business Day, the Federal Funds Rate for such day shall be the average rate quoted to the Administrative Agent on such day as determined by the Administrative Agent.

"**Fee Letter**" means the Fee Letter dated as of March 17, 2010, among the Company, JPMorgan, J.P. Morgan Securities Inc. and Union Bank, N.A.

"**Financial Information**" means the annual report of the Company on Form 10-K for the year ended December 31, 2009, as filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended, and (ii) the Company's current reports on Form 8-K filed January 25, 2010, February 1, 2010, February 19, 2010, March 3, 2010 and March 4, 2010, as so filed.

"**GAAP**" has the meaning given in Section 1(b).

"**Guarantee**" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), *provided* that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "**Guarantee**" used as a verb has a corresponding meaning.

"**Hedge Agreement**" means any interest rate swap, cap or collar agreement, interest rate future or option contract, currency swap agreement, currency future or option contract, commodity future or option contract, commodity forward contract or other similar agreement.

"**Indebtedness**" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"**Indemnified Party**" has the meaning set forth in Section 21.

"**Indenture Trustee**" has the meaning set forth in the first recital hereto.

"**Instruction**" has the meaning set forth in Section 18(b).

"**ISP**" means International Standby Practices 1998 (International Chamber of Commerce Publication No. 590).

"**Issuing Bank**" means JPMorgan and its successors in their capacity as issuer of the Letter of Credit.

"**JPMorgan**" means JPMorgan Chase Bank, N.A., a national banking association, in its individual capacity, and its successors and assigns.

"**LC Disbursement**" has the meaning given in Section 2(a).

"**Letter of Credit**" has the meaning set forth in the third recital hereto.

"**Letter of Credit Commission Rate**" means a rate per annum determined in accordance with Schedule I hereto.

"**LIBO Rate**" means, as of any date of determination, the rate appearing on Reuters Screen LIBOR01 Page (or on any successor or substitute page of such service, or any successor to or substitute for such service, providing rate quotations comparable to those currently provided on such page of such service, as determined by the Administrative Agent from time to time for purposes of providing quotations of interest rates applicable to deposits in dollars in the London interbank market) at approximately 11:00 a.m., London time, on such date of determination, as the rate for deposits in dollars with a one-month maturity. In the event that such rate is not available at such time for any reason, then the "LIBO Rate" shall be the rate at which deposits in dollars in an amount equal to $5,000,000 and for a one-month maturity are offered by the principal London office of the Administrative Agent in immediately available funds in the London interbank market at approximately 11:00 a.m., London time, on such date of determination.

"**Lien**" means any lien, security interest or other charge or encumbrance of any kind, including, without limitation, the lien or retained security title of a conditional vendor and any easement, right of way or other encumbrance on title to real property.

"**Material Subsidiary**" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of April 16, 2010 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"**Maximum Credit Amount**" means, at any date, the Maximum Credit Amount, as defined in the Letter of Credit.

"**Maximum Drawing Amount**" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"**Multiemployer Plan**" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"**1986 Order**" means Decision No. 55120, dated July 24, 1986, of the ACC.

"**Other Taxes**" has the meaning set forth in Section 2(e).

"**Owner Trustee**" has the meaning set forth in the first recital hereto.

"**Parent**" means, as to any Bank, any Person controlling such Bank.

"**Participant**" has the meaning set forth in Section 15(b).

"**Participation**" means a participating interest of a Bank in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a), but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b).

"**Participation Agreement**" has the meaning set forth in the first recital hereto.

"**Participation Amount**" means, with respect to any Bank, the amount set forth in Schedule II hereto opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"**Participation Percentage**" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"**PBGC**" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"**Permitted Lien**" of the Company or any Material Subsidiary means any of the following:

(i) Liens for taxes, assessments or other governmental charges or levies not at the time delinquent or thereafter payable without penalty or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with GAAP shall have been made;

(ii) Liens imposed by or arising by operation of law, such as Liens of carriers, warehousemen, mechanics, materialmen and landlords incurred in the ordinary course of business, including, without limitation, landlord's liens arising under Arizona law under leases entered into by the Company in the 1986 sale and leaseback transactions with respect to PVNGS Unit 2 and securing the payment of rent under such leases, in each case, for sums not overdue for a period of more than 30 days or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with GAAP shall have been made;

(iii) Liens incurred in the ordinary course of business in connection with worker's compensation, unemployment insurance or other forms of governmental insurance or benefits or other similar statutory obligations;

(iv) Liens to secure obligations on surety or appeal bonds;

(v) Liens on cash deposits in the nature of a right of setoff, banker's lien, counterclaim or netting of cash amounts owed arising in the ordinary course of business on deposit accounts, commodity accounts or securities accounts;

(vi) easements, restrictions, reservations, licenses, covenants, and other defects of title that are not, in the aggregate, materially adverse to the use of such property for the purpose for which it is used;

(vii) Liens securing claims against or other obligations of any Person other than the Company or any Subsidiary of the Company neither assumed nor guaranteed by the Company or any Subsidiary of the Company nor on which the Company or any Subsidiary of the Company customarily pays interest, existing upon real estate or rights

in or relating to real estate acquired by the Company or any Subsidiary of the Company for use in the operation of the business of the Company or any Subsidiary of the Company, including, without limitation, for the generation, transmission or distribution of electric energy, transportation, telephonic, telegraphic, radio, wireless or other electronic communication or any other purpose;

(viii) rights reserved to or vested in and Liens on assets arising out of obligations or duties to any municipality or public authority with respect to any right, power, franchise, grant, license or permit, or by any provision of law;

(ix) rights reserved to or vested in others to take or receive any part of the power pursuant to firm power commitment contracts, purchased power contracts, tolling agreements and similar agreements, coal, gas, oil or other minerals, timber or other products generated, developed, manufactured or produced by, or grown on, or acquired with, any property of the Company;

(x) rights reserved to or vested in any municipality or public authority to control or regulate any property of the Company, or to use such property in a manner that does not materially impair the use of such property for the purposes for which it is held by the Company;

(xi) security interests granted in favor of the lessors in the Company's Decommissioning Trust Agreement (PVNGS Unit 2) dated as of January 31, 1992 (such agreement, as amended or otherwise modified from time to time, being the "Unit 2 Trust Agreement") entered into in connection with the PVNGS Unit 2 sale leaseback transaction to secure the Company's obligations in respect of the decommissioning of PVNGS Unit 2 or related facilities;

(xii) Liens that may exist with respect to the Unit 2 Trust Agreement (other than as described in clause (xi) above) or with respect to either of the Company's Decommissioning Trust Agreement (PVNGS Unit 1) or Decommissioning Trust Agreement (PVNGS Unit 3), each dated as of July 1, 1991, as amended or otherwise modified from time to time, relating to the Company's obligation to set aside funds for the decommissioning and retirement from service of such Units;

(xiii) pledges of pollution control bonds and related rights to secure the Company's reimbursement obligations in respect of letters of credit, bond insurance, and other credit or liquidity enhancements supporting pollution control bond transactions, provided that such pollution control bonds are not secured by any other assets of the Company or any Material Subsidiary;

(xiv) rights and interests of Persons other than the Company or any Material Subsidiary (including, without limitation, acquisition rights), related obligations of the Company or any Material Subsidiary and restrictions on it or its property arising out of contracts, agreements and other instruments to which the Company or any Material Subsidiary is a party that relate to the common ownership or joint use of property or other use of property for the benefit of one or more third parties or that allow a third

party to purchase property of the Company or any Material Subsidiary and all Liens on the interests of Persons other than the Company or any Material Subsidiary in such property;

(xv) transfers of operational or other control of facilities to a regional transmission organization or other similar body and Liens on such facilities to cover expenses, fees and other costs of such an organization or body;

(xvi) Liens established on specified bank accounts of the Company to secure the Company's reimbursement obligations in respect of letters of credit supporting commercial paper issued by the Company and similar arrangements for collateral security with respect to refinancings or replacements of the same;

(xvii) rights of transmission users or any regional transmission organizations or similar entities in transmission facilities;

(xviii) Liens on property of the Company sold in a transaction permitted by Section 8(a) hereof to another Person pursuant to a conditional sales agreement where the Company retains title;

(xix) Liens created under this Agreement;

(xx) Liens on cash or cash equivalents not to exceed $200,000,000 (A) deposited in margin accounts with or on behalf of futures contract brokers or paid over to other contract counterparties, or (B) pledged or deposited as collateral to a contract counterparty to secure obligations with respect to (1) contracts (other than for Indebtedness) for commercial and trading activities in the ordinary course of business for the purchase, transmission, distribution, sale, storage, lease or hedge of any energy or energy related commodity or (2) Hedge Agreements;

(xxi) Liens granted on cash or cash equivalents to defease Indebtedness of the Company or any of its Subsidiaries;

(xxii) Liens granted on cash or cash equivalents constituting proceeds from any sale or disposition of assets that is not prohibited by Section 8(a) deposited in escrow accounts or otherwise withheld or set aside to secure obligations of the Company or any Subsidiary providing for indemnification, adjustment of purchase price or any similar obligations, in each case, in an amount not to exceed the amount of gross proceeds received by the Company or any Subsidiary in connection with such sale or disposition;

(xxiii) Liens, deposits and similar arrangements to secure the performance of bids, tenders or contracts (other than contracts for borrowed money), public or statutory obligations, performance bonds and other obligations of a like nature incurred in the ordinary course of business by the Company or any of its Subsidiaries;

(xxiv) rights of lessees arising under leases entered into by the Company or any of its Subsidiaries as lessor, in the ordinary course of business;

(xxv) any Liens on or reservations with respect to governmental and other licenses, permits, franchises, consents and allowances;

(xxvi) Liens on property which is the subject of a Capital Lease Obligation designating the Company or any of its Subsidiaries as lessee and all right, title and interest of the Company or any of its Subsidiaries in and to such property and in, to and under such lease agreement, whether or not such lease agreement is intended as a security;

(xxvii) licenses of intellectual property entered into in the ordinary course of business;

(xxviii) Liens solely on any cash earnest money deposits made by the Company or any of its Subsidiaries in connection with any letter of intent or purchase agreement permitted hereunder;

(xxix) deposits or funds established for the removal from service of operating facilities and coal mines and related facilities or other similar facilities used in connection therewith; and

(xxx) Liens on cash deposits used to secure letters of credit under defaulting lender provisions in credit or reimbursement facilities;

provided, *however*, that no Lien in favor of the PBGC shall, in any event, be a Permitted Lien.

"**Person**" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"**Plan**" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"**Platform**" has the meaning given in Section 7(g).

"**Prime Rate**" means the rate of interest per annum publicly announced from time to time by JPMorgan as its prime rate in effect at its principal office in New York City; each change in the Prime Rate shall be effective from and including the date such change is publicly announced as being effective; provided, however that in the event that there is a successor to JPMorgan in its capacity as Administrative Agent pursuant to Section 20(a)(v), then the term "Prime Rate" as used in this Agreement shall mean the prime rate, base rate or other analogous rate of the new Administrative Agent.

"**PVNGS**" means the Palo Verde Nuclear Generating Station.

"**PWCC**" means Pinnacle West Capital Corporation, an Arizona corporation and its successors.

"**Reimbursement Default**" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"**Reimbursement Event of Default**" has the meaning set forth in Section 9.

"**Related Parties**" means, with respect to any specified Person, such Person's Affiliates and the respective directors, officers, employees, agents and advisors of such Person and such Person's Affiliates.

"**Reportable Event**" means any of the events set forth in Section 4043 of ERISA, other than events for which the 30 day notice period has been waived under the final regulations issued under Section 4043, as in effect as of the date of this Agreement (the "Section 4043 Regulations"). Any changes made to the Section 4043 Regulations that become effective after the Effective Date shall have no impact on the definition of Reportable Event as used herein unless otherwise amended by the Company and the Banks.

"**Required Banks**" means, at any time, Banks with Participation Percentages aggregating more than 50% at such time exclusive of any Defaulting Bank; provided that if after application of such provision, any Bank shall hold more than 50% of the aggregate Participation Percentages of all Banks at such time (and if there is more than one Bank at such time), "Required Banks" shall mean such Bank plus one additional Bank.

"**Sale Leaseback Obligation Bonds**" means PVNGS II Funding Corp.'s (i) 8.00% Secured Lease Obligation Bonds, Series 1993, due 2015; (ii) any other bonds issued by or on behalf of the Company in connection with a sale/leaseback transaction; and (iii) any refinancing or refunding of the obligations specified in subclauses (i) and (ii) above.

"**Standard Letter of Credit Practice**" means, for the Issuing Bank, any domestic or foreign law or letter of credit practices generally and customarily applicable in the city in which the Issuing Bank issued the Letter of Credit other than any such practices that conflict with the express terms of the Letter of Credit or this Agreement. Such practices shall be (i) of banks that regularly issue letters of credit in the particular city and (ii) required or permitted under the ISP.

"**Stated Termination Date**" means April 16, 2013 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17.

"**Subsequent Order**" means any decision, order or ruling of the ACC issued after April 16, 2010 that amends, supersedes or otherwise modifies the 1986 Order or any successor decision, order or ruling.

"**Subsidiary**" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

"**Taxes**" has the meaning set forth in Section 2(e).

"**Termination Date**" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), (v) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the date specified in, and in accordance with, the provisions of the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation.

"**United States**" means the United States of America, including the States and the District of Columbia, but excluding its territories and possessions.

"**Voting Stock**" means capital stock issued by a corporation, or equivalent interests in any other Person, the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of directors (or persons performing similar functions) of such Person, even if the right so to vote has been suspended by the happening of such a contingency.

"**Wholly-Owned Subsidiary**" of any Person means any corporation of which all shares of the issued and outstanding capital stock (other than any director's qualifying shares) having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

(b) Accounting Terms. Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared, in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Company's independent public accountants) with the most recent audited Consolidated financial statements of the Company delivered to the

Administrative Agent ("**GAAP**"). If at any time any change in GAAP or in the interpretation thereof would affect the computation of any financial ratio or requirement set forth in this Agreement, and either the Company or the Required Banks shall so request, the Administrative Agent, the Banks and the Company shall negotiate in good faith to amend such ratio or requirement to preserve the original intent thereof in light of such change in GAAP or in the interpretation thereof (subject to the approval of the Required Banks); provided that, until so amended, such ratio or requirement shall continue to be computed in accordance with GAAP prior to such change therein.

Section 2. *Reimbursement*. (a) Subject to the following sentence, the Company agrees to reimburse the Issuing Bank by making a payment to the Administrative Agent for the account of the Issuing Bank for the full amount of any drawing that the Issuing Bank shall have paid under the Letter of Credit (each an "**LC Disbursement**") prior to or immediately upon making by the Issuing Bank of each such LC Disbursement on the date of each such LC Disbursement; provided that any moneys received from the Company in connection with any LC Disbursement shall be applied solely for the purpose of reimbursement of the related LC Disbursement. If the Company does not reimburse such LC Disbursement in full on or prior to the date such LC Disbursement is made by the times provided for herein, such LC Disbursement shall constitute an advance (a "**Disbursement Advance**"). The Company promises to pay to the Administrative Agent, for the account of the Issuing Bank and, to the extent a Bank made a payment pursuant to Section 14 hereof to reimburse the Issuing Bank, such Bank, each Disbursement Advance on the earliest of (i) the fifth (5th) Business Day after the Issuing Bank shall have made the applicable LC Disbursement and (ii) the Stated Termination Date. The unpaid amount of any Disbursement Advance shall bear interest, for each day from and including the date the LC Disbursement giving rise to such Disbursement Advance is made to but excluding the date that the Company reimburses such Disbursement Advance in full:

(i) from and including the date such relevant LC Disbursement is made until but excluding the earlier of (x) the date the Administrative Agent, for the benefit of the Issuing Bank and, to the extent a Bank made payment pursuant to Section 14 hereof to reimburse the Issuing Bank, such Bank, shall have received reimbursement from the Company of such Disbursement Advance and all unpaid amounts under this clause (i) and (y) the fifth Business Day after such relevant LC Disbursement is made, payable on demand, at a rate per annum equal to the Base Rate plus the Base Rate Margin, and

(ii) together with interest on any amount not paid by the Company when due under clause (i) above, from and including the fifth Business Day after the relevant LC Disbursement is made until such Disbursement Advance is paid in full, payable on demand, at a rate per annum equal to 2% per annum above the Base Rate plus the Base Rate Margin;

provided that such interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law. Interest accrued pursuant to this paragraph shall be for the account of the Issuing Bank, except that interest accrued on and after the date of payment by any Bank pursuant to Section 14 to reimburse the Issuing Bank shall be for the account of such Bank to the extent of such payment.

(b) The Company agrees to pay to the Administrative Agent for the account of the Banks ratably in proportion to their Participation Percentages a letter of credit commission computed at the Letter of Credit Commission Rate on the Maximum Credit Amount of the Letter of Credit from and including the Effective Date to, but excluding, the Termination Date. Such commission accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Effective Date.

(c) The Company agrees to pay to the Administrative Agent for the account of the Issuing Bank a fronting fee at the rate per annum heretofore mutually agreed by the Company and the Issuing Bank pursuant to the Fee Letter, on the Maximum Credit Amount of the Letter of Credit from and including the Effective Date to, but excluding, the Termination Date. Such fronting fee accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Effective Date. The Company agrees to pay to the Issuing Bank for its account (i) on or before the fifth Business Day after the Issuing Bank shall have paid any drawing under the Letter of Credit, a drawing fee (inclusive of any wire-transfer fees) in an amount equal to $135, (ii) on or before the date of any extension of the Letter of Credit pursuant to Section 17, an amendment fee, if any, in an amount mutually agreed upon between the Issuing Bank and the Company, and (iii) on or before the date of any transfer of the Letter of Credit, a transfer fee, if any, in an amount set forth on Exhibit 3 to the Letter of Credit.

(d) (i) If after April 16, 2010, the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by any Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal Reserve System) against letters of credit issued by or assets held by, deposits with or for the account of, or credit extended by, any Bank or shall impose on any Bank any other condition regarding this Agreement or the Letter of Credit or its Participation therein, and the result of any of the foregoing is to increase the cost to such Bank of the issuance or maintenance of the Letter of Credit or its Participation therein, or to reduce the amount of any sum received or receivable by such Bank under this Agreement with respect thereto, by an amount deemed by such Bank to be material, then within 30 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to the Administrative Agent for the account of such Bank such additional amount or amounts as will compensate such Bank for such increased cost or reduction.

(ii) If any Bank shall have determined that, after April 16, 2010, the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change in any such law, rule or regulation, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or

comparable agency, has or would have the effect of reducing the rate of return on capital of such Bank (or its Parent) as a consequence of such Bank's obligations hereunder to a level below that which such Bank (or its Parent) could have achieved but for such adoption, change, request or directive (taking into consideration its policies with respect to capital adequacy) by an amount deemed by such Bank to be material, then from time to time, within 30 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to such Bank such additional amount or amounts as will compensate such Bank (or its Parent) for such reduction.

(iii) Each Bank will notify the Company and the Administrative Agent of any event of which it has knowledge, occurring after April 16, 2010 which will entitle such Bank to compensation pursuant to clause (i) or (ii) of this Section 2(d) as promptly as practicable, but in any event within 90 days after such Bank obtains knowledge thereof; provided that, if such Bank fails to give such notice within 90 days after it obtains knowledge of such an event, such Bank shall, with respect to compensation payable in respect of any costs resulting from such event, only be entitled to payment for costs incurred on and after the date that such Bank does give such notice. A certificate of any Bank claiming compensation under this Section 2(d) and setting forth the additional amount or amounts to be paid to it hereunder shall be conclusive in the absence of demonstrable error. In determining such amount, such Bank may use any reasonable averaging and attribution methods.

(e) For the purposes of this Section 2(e), the following terms have the following meanings:

"**Taxes**" means any and all present or future taxes, duties, levies, imposts, deductions, charges or withholdings with respect to any payment by the Company pursuant to this Agreement, and all liabilities with respect thereto, excluding (i) in the case of each Bank and the Administrative Agent, taxes imposed on or measured by its net income, and franchise or similar taxes imposed on it, by the United States, or by the jurisdiction (or any political subdivision thereof) under the laws of which such Bank or the Administrative Agent (as the case may be) is organized or does business or in which its principal executive office is located or, in the case of each Bank, in which its Applicable Booking Office is located, (ii) any branch profits taxes imposed by the United States or any similar tax imposed by any other jurisdiction in which the Company is located, (iii) any backup withholding that is required by the Internal Revenue Code to be withheld from amounts payable to a Bank that has failed to comply with Section 2(e)(iii)(2)(A), and (iv) in the case of each Bank, any United States withholding tax imposed with respect to any payment by the Company pursuant to this Agreement, but only up to the rate (if any) at which United States withholding tax would apply to such payments to such Bank at the time such Bank first becomes a party to this Agreement.

"**Other Taxes**" means any present or future stamp or documentary taxes and any other excise or property taxes, or similar charges or levies, which arise from any payment made pursuant to this Agreement or from the execution or delivery of, or otherwise with respect to, this Agreement or the Letter of Credit.

(i) Any and all payments by the Company to or for the account of any Bank or the Administrative Agent hereunder shall be made without deduction for any Taxes or Other Taxes; *provided* that, if the Company shall be required by law to deduct any Taxes or Other Taxes from any such payments, (A) the sum payable shall be increased as necessary so that after making all required deductions for any Taxes or Other Taxes (including deductions applicable to additional sums payable under this Section) such Bank or the Administrative Agent (as the case may be) receives an amount equal to the sum it would have received had no such deductions been made, (B) the Company shall make such deductions, (C) the Company shall pay the full amount deducted to the relevant taxation authority or other authority in accordance with applicable law and (D) the Company shall furnish to the Administrative Agent the original or a certified copy of a receipt evidencing payment thereof.

(ii) The Company agrees to indemnify each Bank and the Administrative Agent for the full amount of Taxes or Other Taxes (including, without limitation, any Taxes or Other Taxes imposed or asserted by any jurisdiction on amounts payable under this Section) paid by such Bank or the Administrative Agent (as the case may be) and any liability (including penalties, interest and expenses) arising therefrom or with respect thereto. This indemnification shall be paid within 30 days after such Bank or the Administrative Agent (as the case may be) makes demand therefor. Such demand shall be made as promptly as practicable, but in any event within 90 days after such Bank obtains actual knowledge of such event; *provided*, *however*, that if any Bank fails to make such demand within 90 days after such Bank obtains knowledge of such event, such Bank shall, with respect to compensation payable in respect of such event, not be entitled to compensation in respect of the costs and losses incurred between the 90th day after such Bank obtains actual knowledge of such event and the date such Bank makes such demand.

(iii)

(1) Each Bank shall deliver to the Company and to the Administrative Agent, at the time or times prescribed by applicable laws or when reasonably requested by the Company or the Administrative Agent, such properly completed and executed documentation prescribed by applicable laws or by the taxing authorities of any jurisdiction and such other reasonably requested information as will permit the Company or the Administrative Agent, as the case may be, to determine (A) whether or not payments made hereunder are subject to Taxes, (B) if applicable, the required rate of withholding or deduction, and (C) such Bank's entitlement to any available exemption from, or reduction of, applicable Taxes in respect of all payments to be made to such Bank by the Company pursuant to this Agreement or otherwise to establish such Bank's status for withholding tax purposes in the applicable jurisdiction.

(2) Without limiting the generality of the foregoing:

(A) any Bank that is a "United States Person" within the meaning of Section 7701(a)(30) of the Internal Revenue Code, and not an exempt recipient described in Section 6049(b)(4) of the Internal Revenue Code, shall

deliver to the Company and the Administrative Agent executed originals of Internal Revenue Service Form W-9 or such other documentation or information prescribed by applicable laws or reasonably requested by the Company or the Administrative Agent as will enable the Company or the Administrative Agent, as the case may be, to determine whether or not such Bank is subject to backup withholding or information reporting requirements; and

(B) each Bank that is organized under the laws of a jurisdiction other than the United States (including each State thereof and the District of Columbia) (a "Foreign Bank") that is entitled under the Internal Revenue Code or any applicable treaty to an exemption from or reduction of withholding tax with respect to payments hereunder shall deliver to the Company and the Administrative Agent (in such number of copies as shall be requested by the recipient) on or prior to the date on which such Foreign Bank becomes a Bank under this Agreement (and from time to time thereafter upon the request of the Company or the Administrative Agent, but only if such Foreign Bank is legally entitled to do so), whichever of the following is applicable

(I) executed originals of Internal Revenue Service Form W-8BEN claiming eligibility for benefits of an income tax treaty to which the United States is a party,

(II) executed originals of Internal Revenue Service Form W-8ECI,

(III) executed originals of Internal Revenue Service Form W-8IMY and all required supporting documentation,

(IV) in the case of a Foreign Bank claiming the benefits of the exemption for portfolio interest under section 881(c) of the Internal Revenue Code, (x) a certificate to the effect that such Foreign Bank is not (A) a "bank" within the meaning of section 881(c)(3)(A) of the Internal Revenue Code, (B) a "10 percent shareholder" of the Company within the meaning of section 881(c)(3)(B) of the Internal Revenue Code, or (C) a "controlled foreign corporation" described in section 881(c)(3)(C) of the Internal Revenue Code and (y) executed originals of Internal Revenue Service Form W-8BEN, or

(V) executed originals of any other form prescribed by applicable laws as a basis for claiming exemption from or a reduction in United States Federal withholding tax together with such supplementary documentation as may be prescribed by applicable laws to permit the Company or the Administrative Agent to determine the withholding or deduction required to be made.

(3) Each Bank shall promptly notify the Company and the Administrative Agent of any change in circumstances which would modify or render invalid any claimed exemption or reduction.

(iv) For any period with respect to which a Bank has failed to provide the Company or the Administrative Agent with the appropriate forms pursuant to Section 2(e)(iii) (unless such failure is due to a change in treaty, law or regulation occurring subsequent to the date on which such form originally was required to be provided, but only to the extent that the Bank has complied with the law as changed by such treaty, law or regulation), such Bank shall not be entitled to indemnification under Section 2(e)(ii) or (iii) with respect to Taxes imposed by the United States; *provided* that if a Bank, which is otherwise exempt from or subject to a reduced rate of withholding tax, becomes subject to Taxes because of its failure to deliver a form required hereunder, the Company shall take such steps as such Bank shall reasonably request to assist such Bank to recover such Taxes.

(v) If the Company is required to pay additional amounts to or for the account of any Bank pursuant to this Section, then such Bank will change the jurisdiction of its Applicable Booking Office if, in the reasonable judgment of such Bank, such change (A) will eliminate or reduce any such additional payment which may thereafter accrue and (B) is not otherwise materially disadvantageous to such Bank.

(f) If (x) the Company is required pursuant to Section 2(d) or 2(e) to make any additional payment to any Bank (any Bank so affected an "Affected Bank") or (y) any Bank becomes a Defaulting Bank, the Company may elect to replace the Participation Percentage and Participation of such Affected Bank or Defaulting Bank, as applicable, provided that no Reimbursement Event of Default shall have occurred and be continuing at the time of such replacement, and provided further that, concurrently with such replacement, (i) another bank or other entity which is reasonably satisfactory to the Company, the Issuing Bank and the Administrative Agent shall agree, as of such date, to purchase for cash (to the extent of the principal amount of such Affected Bank's or Defaulting Bank's, as applicable, Disbursement Advances and accrued interest and fees and other reimbursable amounts then due and payable) and otherwise assume the Participation Percentage and Participation of, and other obligations then due to, such Affected Bank or Defaulting Bank, as applicable, pursuant to an Assignment and Assumption and to become a Bank for all purposes under this Agreement and to assume all obligations of such Affected Bank or Defaulting Bank, as applicable, to be replaced as of such date and to comply with the requirements of Section 15 applicable to assignments, (ii) the Company shall pay to such Affected Bank or Defaulting Bank, as applicable, in same day funds on the day of such replacement all interest, fees and other amounts then accrued but unpaid to such Affected Bank or Defaulting Bank, as applicable, by the Company hereunder to and including the date of replacement, including without limitation payments due to such Affected Bank or Defaulting Bank, as applicable, under Sections 2(d) and 2(e), in each case to the extent not paid by the purchasing Bank, and (iii) concurrently with the effectiveness of such replacement, such Affected Bank or Defaulting Bank, as applicable, shall be released with respect to its Participation Percentage, such Participation Percentage shall be terminated, and Disbursement Advances assigned by such Affected Bank or Defaulting Bank, as applicable, and shall cease to be a Bank hereunder but shall continue to be entitled to the benefits of, and subject to, those provisions of this Agreement which survive payment of all amounts payable pursuant to Section 2 and termination of the Letter of Credit and this Agreement.

(g) The Company shall make each payment hereunder to the Administrative Agent at its Chicago office, not later than 2:00 p.m. (New York City time) on the date when due in lawful money of the United States of America and in Federal or other funds immediately available in Chicago. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding day that is a Business Day. If the date for any payment of principal is extended by operation of law or otherwise, interest thereon shall be payable for such extended time.

(h) Computations of the letter of credit commission, the fronting fee referred to in Section 2(c), and interest based on the Prime Rate shall be made by the Administrative Agent on the basis of a year of 365 or 366 days, as the case may be, for the actual number of days (including the first day but excluding the last day) elapsed. Computations of all other interest hereunder shall be made by the Administrative Agent on the basis of a year of 360 days for the actual number of days (including the first day but excluding the last day) elapsed.

(i) Provided that the Company shall have delivered notice thereof to the Administrative Agent not less than three Business Days prior to any proposed termination, the Company may terminate this Agreement (other than those provisions which expressly survive termination hereof) upon (i) payment in full of all amounts payable under Section 2, together with accrued and unpaid interest thereof, (ii) cancellation and return of the Letter of Credit, and (iii) the payment in full of all reimbursable expenses and other obligations under this Agreement together with accrued and unpaid interest thereon. No such termination will be made unless the Equity Participant will be provided with a substitute letter of credit as and to the extent required by the Participation Agreement at such time or unless the Equity Participant shall otherwise consent.

(j) Notwithstanding any provision of this Agreement to the contrary, if any Bank becomes a Defaulting Bank, then the following provisions shall apply for so long as such Bank is a Defaulting Bank:

(i) the Company shall not be required to pay any letter of credit commission to such Defaulting Bank pursuant to Section 2(b) with respect to such Defaulting Bank's Participation Percentage; provided that, without prejudice to any rights or remedies of the Issuing Bank or any Bank hereunder, the letter of credit commission payable under Section 2(b) with respect to such Defaulting Bank's Participation Percentage shall be payable to the Issuing Bank until such Defaulting Lender shall cease to be a Defaulting Lender hereunder. For the avoidance of doubt, it is being understood that, the interest payable by the Company pursuant to Section 2(a) shall continue to be payable to the applicable Banks, including the Defaulting Bank, to the extent the Defaulting Bank has funded its Participation Percentage and would be entitled to such interest had it not become a Defaulting Bank;

(ii) the Participation Percentage of such Defaulting Bank shall not be included in determining whether the Required Banks have taken or may take any action hereunder (including any consent to any amendment or waiver pursuant to Section 10), other than any waiver, amendment or modification requiring the consent of all Banks or of each affected Bank;

(iii) for the avoidance of doubt, the Company shall retain and reserve its other rights and remedies respecting each Defaulting Bank; and

(iv) in the event that the Administrative Agent, the Company and the Issuing Bank each agrees that a Defaulting Bank has adequately remedied all matters that caused such Bank to be a Defaulting Bank, then this Section 2(i) shall no longer apply in respect of such rehabilitated Defaulting Bank.

Section 3. *Amendment and Restatement of Letter of Credit; Conditions to Effectiveness; Transitional Provisions*. (a) On the terms and conditions herein set forth, the Issuing Bank agrees to execute and deliver to the Equity Participant on the Effective Date, or, if all of the conditions precedent to the effectiveness of this Agreement shall not have been satisfied by 3:00 p.m., New York City time, on the Effective Date, on the next succeeding Business Day, the Amended and Restated Letter of Credit substantially in the form of Exhibit A hereto, amending and restating the Existing Letter of Credit.

(b) This Agreement shall become effective on the date (the "**Effective Date**") on which all of the following conditions shall have been satisfied (or waived in accordance with Section 10):

(i) receipt by the Administrative Agent of a counterpart of this Agreement signed by each party hereto;

(ii) receipt by the Administrative Agent of fees payable by the Company on or before the Effective Date in such amounts and for the accounts of such parties as heretofore mutually agreed pursuant to the Fee Letter;

(iii) receipt by the Administrative Agent of evidence to its satisfaction that all amounts accrued and unpaid under the Existing Reimbursement Agreement to (but not including) the Effective Date payable by any party thereto have been paid and the Existing Reimbursement Agreement shall have been terminated;

(iv) receipt by the Administrative Agent of an opinion of Snell & Wilmer L.L.P., special counsel for the Company, dated the Effective Date, in form and substance satisfactory to the Administrative Agent;

(v) receipt by the Administrative Agent of copies, certified by the Secretary, an Associate Secretary or an Assistant Secretary of the Company, of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance of this Agreement and the transactions contemplated hereby;

(vi) receipt by the Administrative Agent of a certificate of the Secretary, an Associate Secretary or an Assistant Secretary of the Company, dated the Effective Date, certifying the names and true signatures of the officers of the Company authorized to sign this Agreement;

(vii) receipt by the Administrative Agent of a certificate, dated the Effective Date, signed by an Authorized Officer to the effect that (x) (A) no Default or Event of

Default under the Facility Lease, and (B) no Reimbursement Default, in each case, shall have occurred and be continuing on the Effective Date or would result from the amendment and restatement of the Letter of Credit pursuant to clause (a) of this Section 3; and (y) that the representations and warranties of the Company set forth in Section 6 of this Agreement shall be true and correct on and as of the Effective Date as though made on and as of such date;

(viii) receipt by the Administrative Agent of certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency, if any, required for the Company to enter into this Agreement;

(ix) receipt by the Administrative Agent of such other approvals, opinions or documents as the Administrative Agent may reasonably request; and

(x) receipt by the Administrative Agent of all documents the Administrative Agent may reasonably request relating to the existence of the Company, the corporate authority for and the validity of this Agreement and any other matters relevant hereto;

provided that all documents (or copies thereof) to be delivered to the Administrative Agent on or before the Effective Date shall be provided to each Bank and shall be in form and substance satisfactory to the Required Banks.

(c) Promptly after this Agreement becomes effective, the Administrative Agent shall give notice thereof and of the Effective Date to each party hereto. Immediately upon the effectiveness of this Agreement, (1) (A) the Existing Letter of Credit shall be deemed to be issued pursuant to this Agreement, (B) the undrawn amount of the Existing Letter of Credit and any unreimbursed amount of disbursements with respect to the Existing Letter of Credit shall be subject to reimbursement hereunder and (C) the provisions of this Agreement shall apply to the Existing Letter of Credit, and the Company and the Banks hereby expressly acknowledge their respective obligations hereunder with respect to the Existing Letter of Credit, and (2) the Issuing Bank will be obligated to amend and restate the Letter of Credit as provided in clause (a) of this Section 3 and each party hereto will be bound by the provisions of this clause (c).

Section 4. *Adjustment of Maximum Drawing Amount; Terms of Drawing*. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

Section 5. *Obligations Absolute*. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement under all circumstances whatsoever, including, without limitation, the following circumstances:

(i) any lack of validity or enforceability or legal effect of this Agreement, the Letter of Credit or any of the Transaction Documents or Financing Documents;

(ii) any amendment or waiver of or any consent to depart from all or any of this Agreement, the Transaction Documents or Financing Documents;

(iii) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant, the Owner Trustee or any transferee of the Letter of Credit (or any persons or entities for whom any of the foregoing may be acting), the Administrative Agent, any Bank, any Participant or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents, the transactions contemplated hereby or thereby or any unrelated transaction; *provided* that nothing herein shall prevent the assertion of such claim by separate suit or compulsory counterclaim;

(iv) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(v) payment by the Issuing Bank under the Letter of Credit against presentation of a certificate which does not comply with the terms of the Letter of Credit; or

(vi) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

Section 6. *Representations and Warranties of the Company*. The Company represents and warrants as of the Effective Date as follows:

(a) Corporate Existence. Each of the Company and each Material Subsidiary: (i) is a corporation duly organized and validly existing under the laws of the jurisdiction of its incorporation; (ii) has all requisite corporate power necessary to own its assets and carry on its business as presently conducted; (iii) has all governmental licenses, authorizations, consents and approvals necessary to own its assets and carry on its business as presently conducted, if the failure to have any such license, authorization, consent or approval is reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, and except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement and except that (A) the Company from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (B) from time to time communities served by the Company may become incorporated and considerable time may elapse before such a franchise is procured, (C) certain such franchises may have expired prior to the renegotiation thereof, (D) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (E) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope); and (iv) is qualified to do business in all jurisdictions in which the nature of the business conducted by it makes such qualification necessary and where failure so to qualify would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. All of the issued and outstanding common stock of the Company is owned by PWCC.

(b) Noncontravention, Etc. The execution, delivery, and performance by the Company of this Agreement are within the Company's corporate powers, have been duly

authorized by all necessary corporate action, and do not (i) contravene the Company's charter or by-laws, (ii) contravene any Applicable Law or any contractual restriction binding on or affecting the Company, or (iii) cause the creation or imposition of any Lien upon the assets of the Company or any Material Subsidiary.

(c) Approvals. No authorization or approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due execution, delivery and performance by the Company of this Agreement, except for (w) the 1986 Order which has been duly issued by the ACC and is in full force and effect in the form originally issued, (x) such other Governmental Actions as have been duly obtained, given or accomplished, (y) the filing with the ACC of a copy of this Agreement within five business days of the execution hereof, in accordance with the 1986 Order and (z) as may be required under Applicable Law not now in effect. The execution, delivery, and performance by the Company of this Agreement do not require the consent or approval of the Equity Participant or the Owner Trustee (except as specified in this Agreement) or PWCC or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been duly obtained, given or accomplished. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or PVNGS Unit 2 is or will be required in connection with the participation by the Administrative Agent, any Bank or any Participant in the consummation of the transactions contemplated by this Agreement, except such Governmental Actions (A) as have been, duly obtained, given or accomplished or (B) as may be required by Applicable Law not now in effect.

(d) Binding Agreement. This Agreement is a legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(e) Litigation. There is no pending or (to the knowledge of an Authorized Officer of the Company) threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator, that, if adversely determined, would be reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(f) Financial Statements. The balance sheet of the Company and its Consolidated Subsidiaries as of December 31, 2009 and the related statements of income and cash flows of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Banks, fairly present in all material respects the financial condition of the Company and its Consolidated Subsidiaries as of such date and the results of operations and cash flows of the Company and its Consolidated Subsidiaries for such fiscal year, all in accordance with GAAP (except as disclosed therein). Since December 31, 2009, there has been no material

adverse change in the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(g) ERISA. The Company and the ERISA Affiliates have fulfilled their respective obligations under the minimum funding standards of ERISA and the Code with respect to each Plan and are in compliance in all material respects with the presently applicable provisions of ERISA and the Code, and have not incurred any liability to the PBGC or any Plan or Multiemployer Plan, other than liability to the PBGC for premiums prior to the due date for such premiums and liability to any Plan maintained by the Company or an ERISA Affiliate or to any Multiemployer Plan for contributions prior to the due date for such contributions which shall be paid in accordance with the provisions of the minimum funding standards of ERISA and the Code.

(h) Taxes. The Company and its Subsidiaries have filed all United States Federal income tax returns and all other material tax returns which are required to be filed by them and have paid all taxes due pursuant to such returns or pursuant to any assessment received by the Company or any of its Subsidiaries, except to the extent that (i) such taxes are being contested in good faith and by appropriate proceedings and appropriate reserves for the payment thereof have been maintained by the Company and its Subsidiaries in accordance with GAAP or (ii) the failure to make such filings or such payments is not reasonably likely to have a material adverse effect on the financial condition or the financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. The charges, accruals and reserves on the books of the Company and its Material Subsidiaries as set forth in the most recent financial statements of the Company delivered to the Banks pursuant to Section 6(f) in respect of taxes and other governmental charges are, in the opinion of the Company, adequate.

(i) Environmental. The operations and properties of the Company and its Subsidiaries comply in all material respects with all environmental laws, the noncompliance with which would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(j) Investment Company. The Company is not an “investment company”, or a company “controlled” by an “investment company”, within the meaning of the Investment Company Act of 1940, as amended.

(k) No Material Misstatements or Omissions. The Financial Information did not as of the date furnished, contain any untrue statement of a material fact or omit to state any material fact necessary to make the statements made therein, in the light of the circumstances under which they were or shall be made, not misleading; provided that with respect to any projected financial information, forecasts, estimates or forward-looking information, the Company represents only that such information and materials have been prepared in good faith on the basis of assumptions believed to be reasonable at the time of preparation of such forecasts, and no representation or warranty is made as to the actual attainability of any such projections, forecasts, estimates or forward-looking information.

(l) No Amendments. Except as provided to the Banks prior to the Effective Date, there has been no amendment or waiver of, or consent with respect to, the payment obligations of the Company under any Transaction Document or Financing Document since March 17, 1993.

Section 7. *Affirmative Covenants*. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will, unless the Required Banks shall otherwise consent in writing:

(a) Preservation of Corporate Existence, Business, Etc. (i) Preserve and maintain its corporate existence, rights (charter and statutory) and franchises (other than "franchises" as described in Arizona Revised Statutes, Section 40-283 or any successor provision) reasonably necessary in the normal conduct of its business, if the failure to maintain such rights and privileges is reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, and use its commercially reasonable efforts to preserve and maintain such franchises reasonably necessary in the normal conduct of its business, except that (A) the Company from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (B) from time to time communities served by the Company may become incorporated and considerable time may elapse before such a franchise is procured, (C) certain such franchises may have expired prior to the renegotiation thereof, (D) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (E) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope; *provided, however*, that the Company may consummate any merger or consolidation permitted under Section 8(b).

(ii) Continue to conduct the same general type of business conducted on April 16, 2010.

(b) Compliance with Laws, Etc. (i) Comply, and cause each Material Subsidiary to comply, in all material respects with all applicable laws, rules, regulations and orders of governmental or regulatory authorities if the failure to comply would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(ii) Comply at all times with the 1986 Order and any Subsequent Order, unless the failure to so comply could not affect the validity or enforceability of the indebtedness of the Company pursuant to this Agreement.

(c) Payment of Taxes and Claims. Pay and discharge, and cause each of its Subsidiaries to pay and discharge, before the same shall become delinquent, all taxes, assessments and governmental charges or levies imposed on it or its property; *provided* that neither the Company nor any of its Subsidiaries shall be required to pay or discharge any such tax, assessment, charge or levy (i) that is being contested in good faith and by proper proceedings and as to which adequate reserves are being maintained in accordance with GAAP or (ii) if the failure to pay such tax, assessment, charge or levy is not reasonably likely to have a material

adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(d) Maintenance of Insurance. Maintain, and cause each Material Subsidiary to maintain, insurance, either with responsible and reputable insurance companies or associations, or through its own program of self-insurance, in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which the Company or such Material Subsidiary operates.

(e) Visitation Rights. Permit, and cause each of its Subsidiaries to permit, at any reasonable time and from time to time, any Bank or any of its agents or representatives to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; *provided* that the Company and its Subsidiaries reserve the right to restrict access to any of its properties in accordance with reasonably adopted procedures relating to safety and security; and provided further that the costs and expenses incurred by any Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions shall be, upon the occurrence and during the continuation of a Reimbursement Default, for the account of the Company and, in all other circumstances, for the account of such Bank.

(f) Keeping of Books; Maintenance of Property. Keep, and cause each Material Subsidiary to keep, (i) proper books of record and account, in which full and correct entries shall be made of all financial transactions and the assets and business of the Company and each such Subsidiary in a manner that permits the preparation of financial statements in accordance with GAAP and (ii) all property useful and necessary in its business in good working order and condition (ordinary wear and tear excepted), it being understood that this covenant relates only to the working order and condition of such properties and shall not be construed as a covenant not to dispose of properties.

(g) Reporting Requirements. Furnish to each of the Banks:

(i) as soon as available and in any event within 60 days after the end of each of the first three fiscal quarters of each fiscal year of the Company, (A) for each such fiscal quarter of the Company, statements of income and cash flows of the Company and its Consolidated Subsidiaries for such fiscal quarter and the related balance sheet of the Company and its Consolidated Subsidiaries as at the end of such fiscal quarter, setting forth in each case in comparative form the corresponding figures for the corresponding fiscal quarter in the preceding fiscal year and (B) for the period commencing at the end of the previous fiscal year and ending with the end of such fiscal quarter, statements of income and cash flows of the Company and its Consolidated Subsidiaries for such period setting forth in each case in comparative form the corresponding figures for the corresponding period in the preceding fiscal year; *provided* that so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(i), its report on Form 10-Q for such fiscal quarter. Each set of financial statements provided under this Section 7(g)(i) shall be accompanied by a

certificate of an Authorized Officer, which certificate shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries in accordance with GAAP, consistently applied (except as disclosed therein), as at the end of, and for, such period (subject to normal year-end audit adjustments);

(ii) as soon as available and in any event within 90 days after the end of each fiscal year of the Company, statements of income, changes in common stock equity and cash flows of the Company and its Consolidated Subsidiaries for such year and the related balance sheets of the Company and its Consolidated Subsidiaries as at the end of such year, setting forth in each case in comparative form the corresponding figures for the preceding fiscal year; *provided* that, so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(ii), its report on Form 10-K for such fiscal year. Each set of financial statements provided pursuant to this Section 7(g)(ii) shall be accompanied by an opinion thereon of independent certified public accountants of recognized national standing, which opinion shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries as at the end of, and for, such fiscal year, in accordance with GAAP consistently applied (except as disclosed therein);

(iii) as soon as possible and in any event within five days after an Authorized Officer knows of the occurrence of any Reimbursement Default continuing on the date of such statement, a statement of an Authorized Officer setting forth details of such Reimbursement Default and the action which the Company has taken and proposes to take with respect thereto;

(iv) as soon as possible, and in any event within ten days after an Authorized Officer knows that any of the events or conditions specified below with respect to any Plan or Multiemployer Plan have occurred or exist, a statement signed by an Authorized Officer setting forth details respecting such event or condition and the action, if any, which the Company or its ERISA Affiliate proposes to take with respect thereto (and a copy of any report or notice required to be filed with or given to the PBGC by the Company or an ERISA Affiliate with respect to such event or condition):

(A) any Reportable Event; *provided* that a failure to meet the minimum funding standard of Section 412 of the Code or Section 302 of ERISA shall be a reportable event regardless of the issuance of any waivers in accordance with Section 412(d) of the Code;

(B) the filing under Section 4041(c) of ERISA of a notice of intent to terminate any Plan in a distress termination or the termination of any Plan in a distress termination;

(C) the institution by the PBGC of proceedings under Section 4042 of ERISA for the termination of, or the appointment of a trustee to administer, any

Plan, or the receipt by the Company or any ERISA Affiliate of a notice from a Multiemployer Plan that such action has been taken by the PBGC with respect to such Multiemployer Plan:

(D) the complete or partial withdrawal by the Company or any ERISA Affiliate under Part 1 of Subtitle E of Title IV of ERISA from a Multiemployer Plan, or the receipt by the Company or any ERISA Affiliate of notice from a Multiemployer Plan that it is in reorganization or insolvency pursuant to Section 4241 or 4245 of ERISA or that it intends to terminate or has terminated under Section 4041A of ERISA; and

(E) the institution of a proceeding by a fiduciary of any Multiemployer Plan against the Company or any ERISA Affiliate to enforce Section 515 of ERISA, which proceeding is not dismissed within 45 days;

(v) promptly after (A) any amendment or modification of the 1986 Order or (B) the promulgation, amendment or modification of any Subsequent Order by the ACC, a copy thereof;

(vi) promptly after the sending or filing thereof, copies of all reports and registration statements (other than exhibits thereto and registration statements on Form S-8 or its equivalent) which the Company or any of its Subsidiaries files with the Securities and Exchange Commission or any national securities exchange;

(vii) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the payment obligations of the Company under any Transaction Document or Financing Document;

(viii) promptly after an Authorized Officer becomes aware of the occurrence thereof, notice of any change by Moody's or S&P of their respective Ratings or of the cessation (or subsequent commencement) by Moody's or S&P of publication of their respective Ratings (as such terms are defined on Schedule I hereto); and

(ix) such other information respecting the condition or operations, financial or otherwise, of the Company or any of its Subsidiaries as the Administrative Agent at the request of any Bank may from time to time reasonably request.

The Company will furnish to the Banks, at the time it furnishes each set of financial statements pursuant to Section 7(g)(i) or 7(g)(ii) above, a certificate of an Authorized Officer (x) to the effect that no Reimbursement Default has occurred and is continuing (or, if any Reimbursement Default has occurred and is continuing, describing the same in reasonable detail and describing the action that the Company has taken and proposes to take with respect thereto) and (y) setting forth in reasonable detail the computations necessary to determine whether the Company is in compliance with Section 8(e) as of the end of the relevant fiscal quarter or fiscal year.

Information required to be delivered pursuant to Sections 7(g)(i), (ii) and (vi) above shall be deemed to have been delivered on the date on which the Company provides notice to the

Administrative Agent that such information has been posted on the Company's parent's website on the Internet at www.pinnaclewest.com, at sec.gov/edaux/searches.htm or at another website identified in such notice and accessible by the Banks without charge; provided that (i) such notice may be included in a certificate delivered pursuant to Section 7(g)(i) or (ii) and (ii) the Company shall deliver paper copies of the information referred to in Section 7(g)(i), (ii), and (vi) to any Bank which requests such delivery. Notwithstanding anything contained herein, in every instance the Company shall be required to provide to the Banks copies (which copies may be in electronic PDF format) of certificates of Authorized Officers required under Section 7(g). Subject to the confidentiality provisions set forth in Section 22, the Company hereby acknowledges that the Administrative Agent may make available to the Banks materials and/or information provided by or on behalf of the Company hereunder (collectively, "**Company Materials**") by posting the Company Materials on IntraLinks or another similar electronic system (the "**Platform**").

(h) Filing with ACC. File a copy of this Agreement, as executed by each of the parties hereto, with the ACC within five business days of the execution hereof.

Section 8. *Negative Covenants*. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will not, without the written consent of the Required Banks:

(a) Sale of Assets. Sell, lease, transfer or otherwise dispose of, or permit any of its Material Subsidiaries to sell, lease, transfer or otherwise dispose of, any assets, or grant any option or other right to purchase, lease or otherwise acquire any assets to any Person other than the Company or any Subsidiary of the Company, except (i) dispositions in the ordinary course of business, including, without limitation, sales or other dispositions of electricity and related and ancillary services, other commodities, emissions credits and similar mechanisms for reducing pollution, and damaged, obsolete, worn out or surplus property no longer required or useful in the business or operations of the Company or any of its Subsidiaries, (ii) sale or other disposition of patents, copyrights, trademarks or other intellectual property that are, in the Company's reasonable judgment, no longer economically practicable to maintain or necessary in the conduct of the business of the Company or its Subsidiaries and any license or sublicense of intellectual property that does not interfere with the business of the Company or any Material Subsidiary, (iii) in a transaction authorized by clause (b) of this Section, (iv) individual dispositions occurring in the ordinary course of business which involve assets with a book value not exceeding $5,000,000, (v) sales of assets during the term of this Agreement having an aggregate book value not to exceed 30% of the total of all assets properly appearing on the most recent balance sheet of the Company provided pursuant to Section 6(f) or 7(g)(ii) hereof and (vi) any Lien permitted under Section 8(c).

(b) Mergers, Etc. Merge or consolidate with or into any Person, or permit any Material Subsidiary to do so, except that:

(i) any Material Subsidiary may merge with any Wholly-Owned Subsidiary of the Company;

(ii) any Material Subsidiary may merge into the Company; and

(iii) the Company may merge with, and any Material Subsidiary may merge with, any other Person;

provided that, in each case, immediately after giving effect to such proposed transaction, no Reimbursement Default would exist; and *provided further* that, in the case of any such merger to which the Company is a party, the Company is the surviving corporation and in the case of any such merger to which any Material Subsidiary and any other Person are the parties, such Material Subsidiary is the surviving corporation.

(c) Negative Pledge. Create or suffer to exist, or permit any of its Material Subsidiaries to create or suffer to exist, any Lien on or with respect to any of its properties, whether now owned or hereafter acquired, or assign, or permit any of its Material Subsidiaries to assign, any right to receive income, other than:

(i) Permitted Liens;

(ii) Liens upon or in, or conditional sales agreements or other title retention agreements with respect to, any real or personal property acquired or held by the Company or any Subsidiary in the ordinary course of business to secure the purchase price of such property, or the construction of or improvements to such property, or to secure Indebtedness incurred solely for the purpose of financing the acquisition, construction or improvement of such property to be subject to such Liens (including any Liens placed on such property within 180 days after the latest of the acquisition, completion of construction or improvement of such property), or Liens existing on such property at the time of its acquisition (other than any such Liens created in contemplation of such acquisition that were not incurred to finance the acquisition of such property) or extensions, renewals, refundings or replacements of any of the foregoing for the same or a lesser amount, provided, however, that no such Lien shall extend to or cover any properties of any character other than the property being acquired, constructed or improved and proceeds, improvements and replacements thereof and no such extension, renewal, refunding or replacement shall extend to or cover any properties not theretofore subject to the Lien being extended, renewed, refunded or replaced;

(iii) assignments of the right to receive income, and Liens on property, of a Person existing at the time such Person is merged into or consolidated with the Company or any Subsidiary of the Company or becomes a Subsidiary of the Company;

(iv) Liens with respect to the leases and related documents entered into by the Company in connection with PVNGS Unit 2 and Liens with respect to the leased interests and related rights if the Company reacquires ownership in any of those interests or acquires any of the equity or owner participants' interests in the trusts that hold title to such leased interests, whether or not it also directly assumes the Sale Leaseback Obligation Bonds, and Liens on the Company's interests in the trusts that hold title to such leased interests and related rights in the event that the Company acquires any of the equity or owner participants' interests in such trusts pursuant to a "special transfer" under

the Company's existing PVNGS Unit 2 sale and leaseback transactions and any Liens resulting or deemed to have resulted if the PVNGS Unit 2 leases are required to be accounted for as capital leases in accordance with GAAP;

(v) other assignments of the right to receive income and Liens securing Indebtedness or claims in an aggregate principal amount not to exceed 20% of the Company's total assets as stated on the most recent balance sheet of the Company provided pursuant to Section 6(f) and 7(g) hereof at any time outstanding; and

(vi) the replacement, extension or renewal of any Lien permitted by clause (iii) or (iv) above upon or in the same property theretofore subject thereto or the replacement, extension or renewal (without increase in the amount or change in any direct or contingent obligor) of the Indebtedness secured thereby.

(d) Assignment of Transaction Documents or Financing Documents. Enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents.

(e) Indebtedness. Permit Consolidated Indebtedness to exceed 65% of Consolidated Capitalization at any time.

"**Consolidated**" refers to the consolidation of accounts in accordance with GAAP.

"**Consolidated Capitalization**" means, at any date, the sum as of such date of Consolidated Indebtedness and Consolidated Net Worth.

"**Consolidated Indebtedness**" means, at any date, the Indebtedness of the Company and its Consolidated Subsidiaries determined on a Consolidated basis as of such date.

"**Consolidated Net Worth**" means, at any date, the sum as of such date of (a) the par value (or value stated on the books of the Company) of all classes of capital stock of the Company and its Subsidiaries, excluding the Company's capital stock owned by the Company and/or its Subsidiaries, plus (or minus in the case of a surplus deficit) (b) the amount of the Consolidated surplus, whether capital or earned, of the Company, determined in accordance with GAAP as of the end of the most recent calendar month (excluding the effect on the Company's accumulated other comprehensive income/loss of the ongoing application of Accounting Standards Codification Topic 815).

Section 9. *Reimbursement Events of Default*. If any of the following events ("**Reimbursement Events of Default**") shall occur and be continuing:

(i) The Company shall fail to pay when due any amount payable under Section 2(a) or fail to pay any other amount payable under Section 2 within five (5) Business Days after the same becomes due and payable; or

(ii) The Company shall fail to perform or observe (A) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 8(a), 8(b), 8(c) or 8(e), or (B) any term, covenant or agreement contained in this Agreement (other than those covered by

clause (i) above or subclause (A) of this clause (ii) or Section 7(e) or Section 19) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(iii) Any representation or warranty made by the Company herein or by the Company (or any of its officers) in any certificate delivered in connection with this Agreement shall prove to have been false or misleading in any material respect when made; or

(iv) Any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) (A) The Company or any of its Material Subsidiaries shall fail to pay (1) any principal of or premium or interest on any Indebtedness that is outstanding in a principal amount of at least $35,000,000 in the aggregate (but excluding Indebtedness outstanding hereunder), or (2) an amount, or post collateral as contractually required in an amount, of at least $35,000,000 in respect of any Hedge Agreement, of the Company or such Material Subsidiary (as the case may be), in each case, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness or Hedge Agreement; or (B) any event of default shall exist under any agreement or instrument relating to any such Indebtedness and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such event is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(vi) The Company or any of its Material Subsidiaries shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least $35,000,000, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(vii) The Company or any of its Material Subsidiaries shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company or any of its Material Subsidiaries seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any Debtor Relief Law, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it

(but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company or any of its Material Subsidiaries shall take any corporate action to authorize any of the actions set forth above in this clause (vii); or

(viii) Judgments or orders for the payment of money that exceeds any applicable insurance coverage (the insurer of which shall be rated at least "A" by A.M. Best Company) by more than $35,000,000 in the aggregate shall be rendered against the Company or any Material Subsidiary and such judgments or orders shall continue unsatisfied or unstayed for a period of 45 days; or

(ix) (A) Any "person" or "group" (as such terms are used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended, but excluding any employee benefit plan of such person or its subsidiaries, and any person or entity acting in its capacity as trustee, agent or other fiduciary or administrator of any such plan) becomes the "beneficial owner" (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, as amended), directly or indirectly, of 30% or more of the equity securities of PWCC entitled to vote for members of the board of directors of PWCC; or (B) during any period of 24 consecutive months, a majority of the members of the board of directors of PWCC cease (other than due to death or disability) to be composed of individuals (1) who were members of that board on the first day of such period, (2) whose election or nomination to that board was approved by individuals referred to in clause (1) above constituting at the time of such election or nomination at least a majority of that board or (3) whose election or nomination to that board was approved by individuals referred to in clauses (1) and (2) above constituting at the time of such election or nomination at least a majority of that board; or (C) PWCC shall cease for any reason to own, directly or indirectly 80% of the Voting Stock of the Company; or

(x) An event or condition specified in Section 7(g)(iv) shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the foregoing) which is, in the determination of the Required Banks, likely to exceed $35,000,000 in the aggregate; or

(xi) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(xii) any event specified in subsection (vii), (viii) or (x) of Section 15 of the Facility Lease shall occur; or

(xiii) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding $1,000,000 within the periods specified in that Section.

then, in every such event the Issuing Bank may, and if instructed to do so by the Required Banks the Issuing Bank shall, by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein. The Administrative Agent shall give notice to the Company under Section 9(ii) promptly upon being requested to do so by the Required Banks and will promptly notify each Bank of any such notice given at the request of the Required Banks.

Section 10. *Amendments and Waivers*. No modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any consent to the assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents shall be effective unless the same shall be in writing and signed by (or with the written consent of) the Company and the Required Banks (and, if the rights or duties of the Issuing Bank or the Administrative Agent are affected thereby, by it); provided that no such modification, amendment, waiver or consent shall, unless signed by (or with the written consent of) each Bank affected thereby, (i) increase the Maximum Credit Amount or Maximum Drawing Amount or subject any Bank to any additional obligation under this Agreement or the Letter of Credit, (ii) reduce the principal of or rate of interest on any reimbursement obligation or reduce the letter of credit commission payable under Section 2(b), (iii) postpone the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission, (iv) extend the Stated Termination Date or the Termination Date or (v) change the definition of Required Banks or the provisions of this Section 10 or any provision of this Agreement that requires action by all the Banks. Any waiver of any provision of this Agreement or the Letter of Credit shall be effective only in the specific instance and for the specific purpose for which given.

Section 11. *Notices*. (a) All notices, requests, demands and other communications provided for hereunder shall, unless otherwise stated herein, be in writing (including facsimile transmission, electronic transmission (subject to Section 11(c) below), or similar transmission) and mailed, sent or delivered:

(i) if to the Company, in the case of deliveries, to its street address at 400 North Fifth Street, Phoenix, Arizona 85004; in the case of mailings, to its mailing address at P.O. Box 53999, Phoenix, Arizona 85072-3999, and in the case of facsimile transmission, to telecopy no. (602) 250-5640, in each case to the attention of the Treasurer; and in the case of electronic mail, to lee.nickloy@pinnaclewest.com;

(ii) if to the Administrative Agent, in the case of deliveries or mailings, to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-0090, Chicago, IL 60603, and in the case of facsimile transmission, to telecopy no. (312) 732-1762, in each case to the attention of Nancy Barwig; and in the case of electronic mail, to nancy.r.barwig@jpmorgan.com; with a copy to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-0874, Chicago, IL 60603, and in the case of facsimile transmission, to telecopy no. (312) 325-3150, in each case to the attention of Lisa Tverdek; and in the case of electronic mail, to lisa.tverdek@jpmorgan.com;

(iii) if to the Issuing Bank, in the case of deliveries or mailings, to its address at JPMorgan Chase Bank, N.A., 300 South Riverside Plaza, Mail Code IL1-0236, Chicago, IL 60606-0236, Attention: Standby Letter of Credit Unit, and in the case of facsimile transmission, to telecopy no. (312) 233-2266 and telephone No.: (800) 634-1969, Option 1, in each case to the attention of Manager – Immediate Action Required; and in the case of electronic mail, to standbylc.chi.mc@jpmchase.com; with a copy to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-1650, Chicago, IL 60603, and in the of case facsimile transmission, to telecopy no. (312) 732-2729 and telephone no. (312) 732-2592, in each case to the attention of Phyllis Huggins; and in the case of electronic mail, to phyllis.huggins@jpmorgan.com;

(iv) if to any other Bank, at such address, electronic mail address, or telecopy number as shall be designated by it in its Administrative Questionnaire;

or, as to each party, to such other person and/or to such other address or number as shall be designated by such party in a written notice to each other party. All such notices, requests, demands and other communications shall be effective when mailed or sent, addressed as aforesaid (subject to Section 11(c) below in the case of electronic communications), except that notices to the Administrative Agent shall not be effective until received by the Administrative Agent and any notice to the Equity Participant pursuant to Section 9 shall not be effective until received by the Equity Participant. Notices of any Reimbursement Default shall be sent by the Company to the Administrative Agent by facsimile transmission.

(b) As promptly as practicable after receipt by the Administrative Agent of any notice or other communication delivered hereunder by the Company, the Administrative Agent shall furnish a copy thereof to each Bank, to the extent such notice or other communication is not otherwise required by the terms thereof to be delivered by the Company to each Bank.

(c) Notices and other communications to the Administrative Agent, the Banks and the Issuing Bank hereunder may be delivered or furnished by electronic communications (including e-mail and internet or intranet websites) pursuant to procedures approved by the Administrative Agent and agreed by the Company; *provided* that the foregoing shall not apply to notices pursuant to Sections 2, 14 or 17 unless otherwise agreed by the Administrative Agent and the applicable Bank or to notices pursuant to the Letter of Credit. The Administrative Agent and the Company may, each in its discretion, agree to accept notices and other communications to it hereunder by electronic communications pursuant to procedures approved by it; *provided* that approval of such procedures may be limited to particular notices or communications. Unless the Administrative Agent and the Company shall otherwise agree, notices and other communications sent to an electronic mail address shall be deemed received upon the sender's receipt of an acknowledgement from the intended recipient (such as by the "return receipt requested" function, as available, return electronic mail or other written acknowledgement); *provided* that (x) if such notice or other communication is not sent during the normal business hours of the recipient, such notice or communication shall be deemed to have been sent at the opening of business on the next business day for the recipient, and (y) notices or communications posted to an Internet website shall be deemed received upon the deemed receipt by the intended recipient at its electronic mail address as described in immediately foregoing clause (x) of notification that such notice or communication is available and identifying the website address therefor.

(d) The Platform is provided "as is" and "as available." The Agent Parties (as defined below) do not warrant the accuracy or completeness of the Company Materials or the adequacy of the Platform, and expressly disclaim any liability for errors in or omissions from the Company Materials. No warranty of any kind, express or implied or statutory, is made by any Agent Party in connection with the Company Materials or the Platform. In no event shall the Administrative Agent, its Affiliates, or any partners, directors, officers, employees, agents and advisors of the Administrative Agent or of its Affiliates (collectively, the "**Agent Parties**") have any liability to the Company, any Bank or any other Person for losses, claims, damages, liabilities or expenses of any kind (whether in tort, contract or otherwise) arising out of the Company's or the Administrative Agent's transmission of Company Materials through the Internet, except to the extent that such losses, claims, damages, liabilities or expenses are determined by a court of competent jurisdiction by a final and nonappealable judgment to have resulted from the gross negligence or willful misconduct of such Agent Party.

Section 12. *No Waiver; Remedies*. No failure on the part of the Administrative Agent or any Bank to exercise, and no delay in exercising, any right, power, or privilege hereunder shall operate as a waiver thereof; nor shall any single or partial exercise of any right hereunder preclude any other or further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

Section 13. *Waiver of Right of Setoff*. The Administrative Agent and each Bank hereby waive any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by it to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "**bankruptcy events**"), against any and all of the obligations of the Company now or hereafter existing in respect of any reimbursement obligation of the Company set forth in Section 2(a), *provided* that any such waiver shall be deemed ineffective as and to the extent that the Administrative Agent and each Bank receive, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience (which counsel shall be mutually satisfactory to the Administrative Agent and the Equity Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Administrative Agent or any Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section 13 shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section 13.

Section 14. *Participations of the Banks*. (a) The Issuing Bank hereby sells to each other Bank, and each Bank hereby severally purchases from the Issuing Bank, as of the Effective Date, a Participation in an amount equal to such Bank's Participation Percentage of the Letter of Credit and in each drawing thereunder, all on the terms and conditions set forth herein. Each Bank

acknowledges and agrees that its obligation to acquire participations pursuant to this paragraph in respect of the Letters of Credit is absolute and unconditional and shall not be affected by any circumstance whatsoever, including any amendment, renewal or extension of the Letter of Credit or the occurrence and continuance of a Reimbursement Event of Default, and that each such payment shall be made without any offset, abatement, withholding or reduction whatsoever.

(b) If at any time on or after the Effective Date the Company shall fail to reimburse any LC Disbursement prior to or immediately upon making thereof by the Issuing Bank, such LC Disbursement shall constitute a Disbursement Advance in accordance with Section 2(a), and the Administrative Agent shall promptly (but in any event no later than 2:30 p.m., New York City time, on the date payment is due from the Banks under this Section 14(b)) advise each Bank thereof and of the amount due from the Company and the amount of such Bank's Participation therein, and each Bank shall pay, no later than 4:00 p.m. (New York City time) on such date such Bank's Participation Percentage of such amount by transferring the same in immediately available funds to the Administrative Agent for the account of the Issuing Bank at the Administrative Agent's address specified in Section 11. With respect to any such LC Disbursement, each Bank agrees that the Issuing Bank shall have no responsibility to the Banks other than obtaining the certificates referred to in the Letter of Credit and notifying each Bank thereof. The Administrative Agent shall promptly credit each Bank's account with such Bank's Participation Percentage of (i) all amounts representing principal of, or interest on, any Disbursement Advances, in each case in respect of which such Bank has funded its Participation Percentage in accordance with the foregoing provisions of this Section 14(b) and (ii) letter of credit commissions payable to each Bank pursuant to Section 2(b) of this Agreement and accruing on and after the Effective Date, but, in the case of both clause (i) and clause (ii), only if, when and to the extent received by the Administrative Agent from the Company. All such payments shall be made if, when and to the extent the Administrative Agent receives payment from the Company in respect of any Disbursement Advance and of the letter of credit commission pursuant to Section 2(b) of this Agreement, and in the same funds in which such amounts are received, by credit to an account at a bank located in the United States of America as each Bank shall designate in writing to the Administrative Agent.

(c) If the Administrative Agent should for any reason make any payment to any Bank in anticipation of the receipt of funds from the Company and such funds are not received by the Administrative Agent from the Company on the date payment is due, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such amounts transferred to such Bank by the Administrative Agent in respect of such Bank's Participation plus interest thereon from the day such amounts were transferred by the Administrative Agent to such Bank to but not including the day such amounts are returned by such Bank at a rate per annum equal to the Federal Funds Rate. If the Administrative Agent is required at any time to return to the Company or to a trustee, receiver, liquidator, custodian or other similar official any portion of the payments made by the Company to the Administrative Agent for the account of any Bank, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such payments transferred to such Bank by the Administrative Agent in respect of such Bank's Participation, but without interest on such payments (unless the Administrative Agent is required to pay interest on such amounts to the Person recovering such payments).

(d) Each Bank agrees that if it should receive any amount due to it under this Agreement in respect of its Participation other than from the Administrative Agent, such Bank will remit all of the same to the Administrative Agent to distribute to the Banks pursuant to this Agreement, and such Bank's Participation shall be adjusted to reflect such remittance. Each Bank further agrees to send the Administrative Agent a copy of any notice sent by such Bank to the Company hereunder.

(e) Each Bank acknowledges and represents that it has made its own independent appraisal of the Company, and the business, affairs and financial condition of the Company, based on such documents and information as such Bank has deemed appropriate, and each Bank will continue to be responsible for making its own independent appraisal of such matters, based on such documents and information as such Bank shall deem appropriate at the time, and has not relied upon and will not hereafter rely upon the Administrative Agent or any other Bank or any information prepared, distributed or otherwise made available by the Administrative Agent for such appraisal or other assessment or review of the Company. Each Bank represents, and in granting a Participation to such Bank it is specifically understood and agreed, that such Bank is acquiring its Participation in the Letter of Credit for its own account in the ordinary course of its commercial banking business and not with a view to, or for sale in connection with, any distribution thereof.

Section 15. *Assignees; Participants*. (a) Each Bank shall have the right, with the prior written consent of the Company (which shall not be unreasonably withheld, and shall not be required if a Reimbursement Event of Default has occurred and is continuing) and the prior written consent of the Administrative Agent and the Issuing Bank, to assign all or a pro rata portion of all of its rights and obligations under its Participation at any time and from time to time to one or more Eligible Institutions (each an "**Assignee**"); *provided* that (i) each such Assignee shall assume such rights and obligations and agree, for the benefit of each other party hereto, to be bound by the provisions of, and perform the obligations of a Bank under, this Agreement, pursuant to an Assignment and Assumption and (ii) the aggregate amount of the Participation or Participations assigned to each such Assignee pursuant to this Section 15(a) shall not be less than $5,000,000. Each Bank shall give prompt notice to the Administrative Agent and the Company of each such assignment made by it. For the avoidance of doubt, no assignment by JPMorgan pursuant to this Section 15 shall affect its rights and obligations in its capacity as Issuing Bank.

(b) (i) Each Bank shall also have the right, without the consent of the Company, to grant participating interests in its Participation at any time and from time to time to one or more other financial institutions or other Persons (other than a natural person or the Company or any of the Company's Affiliates or Subsidiaries) (each a "**Participant**"); *provided* that (A) such Bank's obligations under this Agreement shall remain unchanged, (B) such Bank shall remain solely responsible to the other parties hereto for the performance of such obligations and (C) the Company, the Administrative Agent and the other Banks shall continue to deal solely and directly with such Bank in connection with such Bank's rights and obligations under this Agreement. Each such participation granted by a Bank shall be evidenced by a participation agreement in form acceptable to such Bank. Each such participation agreement shall provide that such Bank shall retain the sole right to exercise its rights under this Agreement and to enforce the obligations owed to it hereunder pursuant to its Participation including, without

limitation, the right to consent to any modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents; *provided* that any such participation agreement may provide that such Bank will not, without the consent of the Participant, consent to any modification, amendment or waiver of this Agreement or the Letter of Credit that (w) increases the Maximum Credit Amount or Maximum Drawing Amount or subjects such Bank to any additional obligation under this Agreement or the Letter of Credit, (x) reduces the principal of or rate of interest on any reimbursement obligation or reduces the letter of credit commission payable under Section 2(b), (y) postpones the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission or (z) extends the Stated Termination Date or the Termination Date, in each case subject to such participation.

(ii) Subject to clause (iii) below, the Company agrees that each Participant shall be entitled to the benefits of Sections 2(d) and 2(e) to the same extent as if it were a Bank and had acquired its interest by assignment pursuant to Section 15(a).

(iii) A Participant shall not be entitled to receive any greater payment under Section 2(d) or 2(e) than the applicable Bank would have been entitled to receive with respect to the participating interest granted to such Participant, unless the granting of such interest to such Participant is made with the Company's prior written consent. A Participant organized under the laws of a jurisdiction outside the United States shall not be entitled to the benefits of Section 2(d) or 2(e) unless the Company is notified of the participating interest granted to such Participant and such Participant agrees, for the benefit of the Company, to comply with Section 2(d) or 2(e) as though it were a Bank.

Section 16. *Continuing Obligation; Binding Effect*. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date and (ii) the date upon which all amounts due and owing to the Administrative Agent or any Bank hereunder shall have been paid in full. The obligation of the Company to reimburse the Administrative Agent, the Issuing Bank and the Banks pursuant to Sections 2(d), 2(e), 19 and 21 hereof and the obligations of the parties pursuant to Sections 22, 24 and 27 hereof shall survive the termination of the Letter of Credit and this Agreement. This Agreement shall be binding upon and inure to the benefit of each of the parties hereto and their respective successors. The Company shall not have the right to assign its rights hereunder or any interest herein to any Person without the prior written consent of the Issuing Bank and each Bank. The Issuing Bank shall not have the right to assign its rights as the Issuing Bank hereunder without the prior written consent of the Company (which shall not be unreasonably withheld) and each Bank.

Section 17. *Extension of the Letter of Credit*. At least 105 days but not more than 180 days before the Stated Termination Date, the Company may request the Administrative Agent in writing (each such request being irrevocable and binding), with a copy to the Issuing Bank and each Bank, to extend for not less than three years, nor more than eight years (or, if earlier, the end of the Basic Lease Term or as otherwise required under the Participation Agreement), the Stated Termination Date, specifying the terms and conditions, including fees, to be applicable to such extension. Within 45 days after receiving such extension request (or such later date as the Company may authorize in writing, but in no event later than 60 days before the Stated

Termination Date), each Bank shall notify the Administrative Agent and the Company of its consent or nonconsent to such extension request, and if any Bank shall give no such notice, it shall be deemed not to have consented to such extension request. No such requested extension shall be effective without the consent of all the Banks. The consent of any Bank shall be in its sole discretion and shall be conditional upon no Reimbursement Default or Reimbursement Event of Default existing as of the date of such extension and the preparation, execution and delivery of legal documentation in form and substance satisfactory to such Bank and its counsel, incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement among the Company, and the Banks, and evidence satisfactory to it of the due authorization and validity thereof.

Section 18. *Limited Liability of the Banks*.

(a) The Company assumes all risks of the acts or omissions of the Equity Participant and any beneficiary or transferee of the Letter of Credit with respect to its use of the Letter of Credit. None of the Administrative Agent, the Issuing Bank and the Banks, nor their respective Affiliates nor any officer, director, employee or agent of any of the foregoing shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or any acts or omissions of the Equity Participant or any beneficiary or transferee in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement thereon, even if such documents shall prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Issuing Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except that the Company shall have a claim against the Issuing Bank, and the Issuing Bank shall be liable to the Company, to the extent, but only to the extent, of any direct, as opposed to special, indirect, consequential or punitive, damages or losses suffered by the Company which the Company proves were caused by the Issuing Bank's gross negligence or willful misconduct in (i) honoring a presentation that does not strictly comply with the Letter of Credit, (ii) failing to honor a presentation that strictly complies with the Letter of Credit or (iii) retaining any document presented for purposes of drawing under the Letter of Credit. In no event shall the Issuing Bank be deemed to have failed to act with due diligence or reasonable care if the Issuing Bank's conduct is in accordance with Standard Letter of Credit Practice and in accordance with this Agreement. In furtherance and not in limitation of the foregoing, the Issuing Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Issuing Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

(b) Without limiting any other provision of this Agreement, the Issuing Bank and each other Indemnified Party (if applicable), shall not be responsible to the Company for, and the Issuing Bank's rights and remedies against the Company and the Company's obligation to reimburse the Issuing Bank shall not be impaired by: (i) honor of a presentation under the Letter of Credit which on its face strictly complies with the terms of the Letter of Credit; (ii) honor of a presentation of any documents presented for purposes of drawing under the Letter of Credit (a "**Drawing Document**") which appear on their face to have been signed, presented or issued (X)

by any purported successor or transferee of any beneficiary or other party required to sign, present or issue the Drawing Documents or (Y) under a new name of the beneficiary; (iii) acting upon any communication or instruction (whether oral, telephonic, written, telegraphic, facsimile or electronic) (each an "**Instruction**") that is unauthorized and that is (x) received pursuant to the express terms of the Letter of Credit or (y) any other Instruction regarding the Letter of Credit or error in computer transmission that in either case the Indemnified Party, in Good Faith, believes to have been given by a Person or entity authorized to give such Instruction; (iv) any errors, omissions, interruptions or delays in transmission or delivery of any message, advice or document (regardless of how sent or transmitted) or for reasonable errors in interpretation of technical terms made in good faith after advice of counsel or in translation; (v) any delay in giving or failing to give any notice; (vi) any acts, omissions or fraud by, or the solvency of, any beneficiary, any nominated Person or any other Person other than the Issuing Bank or an Indemnified Party; (vii) any breach of contract between the beneficiary and the Company or any of the parties to the underlying transaction; (viii) assertion or waiver of any provision of the ISP which primarily benefits an issuer of a letter of credit, including, any requirement that any Drawing Document be presented to it at a particular hour or place, except to the extent such provisions of the ISP conflict with the express provisions of the Letter of Credit or this Agreement; (ix) dishonor of any presentation for which the Company is unable or unwilling to reimburse or indemnify the Issuing Bank (provided that the Company acknowledges that if the Issuing Bank shall later be required to honor the presentation, the Company shall be liable therefor in accordance with Article 2 hereof); and (x) acting or failing to act as required or permitted under Standard Letter of Credit Practice. For purposes of this Section 18(b), "**Good Faith**" means honesty in fact in the conduct of the transaction concerned. For the avoidance of doubt, it is understood that this Section 18(b) shall not be construed to limit the Issuing Bank's liability for damages caused by the Issuing Bank's gross negligence or willful misconduct as otherwise provided for in this Agreement.

(c) The Company shall notify the Administrative Agent and the Issuing Bank of (i) any noncompliance with any Instruction given by the Company with respect to the Letter of Credit or any amendment thereto, any other irregularity with respect to the text of the Letter of Credit or any amendment thereto or any claim of an unauthorized, fraudulent or otherwise improper Instruction given by the Company with respect to the Letter of Credit or any amendment thereto, in each case within ten (10) Business Days after an Authorized Officer of the Company becomes aware of the receipt by the Company of a copy of the Letter of Credit or any such amendment and (ii) any objection the Company may have to the Issuing Bank's honor or dishonor of any presentation under the Letter of Credit or any other action or inaction taken or proposed to be taken by the Issuing Bank under or in connection with this Agreement or the Letter of Credit, within ten (10) Business Days after an Authorized Officer of the Company becomes aware of the objectionable action or inaction. To the extent allowed by applicable law, the failure to so notify the Issuing Bank within said times shall discharge the Issuing Bank from any loss or liability that the Issuing Bank could have avoided or mitigated had it received such notice, to the extent that the Issuing Bank could be held liable for damages hereunder; provided that the foregoing shall not be construed to excuse the Issuing Bank from liability to the Company to the extent of any direct damages (as opposed to consequential damages, claims in respect of which are hereby waived by the Company to the extent permitted by applicable law) suffered by the Company that are caused by the Issuing Bank's failure to exercise care when determining whether drafts and other documents presented under the Letter of Credit comply

with the terms thereof or by the Issuing Bank's gross negligence or willful misconduct; provided, further, that, if the Company shall not provide such notice to the Issuing Bank within twenty (20) Business Days of the date of receipt, the Issuing Bank shall have no liability whatsoever for such noncompliance, irregularity, action or inaction and the Company shall be precluded from raising such noncompliance, irregularity or objection as a defense or claim against Issuing Bank. For the avoidance of doubt, it is understood that this Section 18(c) shall not be construed to limit the Issuing Bank's liability for damages caused by the Issuing Bank's gross negligence or willful misconduct as otherwise provided for in this Agreement.

Section 19. *Cost, Expenses and Taxes*. The Company agrees to pay not later than 30 days after demand therefor (a) all reasonable costs and expenses of the Administrative Agent in connection with the preparation, execution, delivery, filing, recording and administration of this Agreement and any other documents which may be delivered in connection with this Agreement and any waiver or consent under, or amendment of, this Agreement, the Fee Letter or any of the Transaction Documents or Financing Documents, including, without limitation, the reasonable fees and out-of-pocket expenses of one firm of attorneys for the Administrative Agent (and any additional firms required to address matters in respect of which such firm is precluded from representation as a result of conflicts) and local counsel who may be retained by said counsel, with respect thereto and with respect to advising the Administrative Agent as to its rights and responsibilities under this Agreement; (b) as to the Administrative Agent, the Issuing Bank and each Bank, all reasonable costs and expenses (including reasonable counsel fees and expenses) in connection with (i) the enforcement of this Agreement and such other documents which may be delivered in connection with this Agreement or (ii) any action or proceeding relating to a court order, injunction or other process or decree restraining or seeking to restrain the Issuing Bank from paying any amount under the Letter of Credit; and (c) as to the Administrative Agent and the Issuing Bank, all reasonable costs and expenses (including reasonable counsel fees and expenses) in connection with each transfer of the Letter of Credit in accordance with its terms. In addition, the Company shall pay any and all stamp, documentary, filing, recording or other similar taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents, and agrees to save the Administrative Agent and each Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, *provided* that the Administrative Agent and each Bank agree promptly to notify the Company of any such taxes and fees which are incurred by the Administrative Agent or such Bank. To the extent permitted by applicable law, the foregoing provisions shall supersede any costs and expenses provisions set forth in Section 8.02 of the ISP.

Section 20. *Administrative Agent; Issuing Bank*. (a)

(i) Each Bank irrevocably appoints and authorizes the Administrative Agent to take such action as agent on its behalf and to exercise such powers under this Agreement as are delegated to the Administrative Agent by the terms hereof, together with all such powers as are reasonably incidental thereto.

(ii) The Administrative Agent shall not have any duties or obligations except those expressly set forth herein. Without limiting the generality of the foregoing, (a) the Administrative Agent shall not be subject to any fiduciary or other implied duties, regardless of

whether a Reimbursement Event of Default has occurred and is continuing, (b) the Administrative Agent shall not have any duty to take any discretionary action or exercise any discretionary powers, except discretionary rights and powers expressly contemplated herein that the Administrative Agent is required to exercise in writing as directed by the Required Banks (or such other number or percentage of the Banks as shall be necessary under the circumstances as provided in Section 10), and (c) except as expressly set forth herein, the Administrative Agent shall not have any duty to disclose, and shall not be liable for the failure to disclose, any information relating to the Company or any of its Subsidiaries that is communicated to or obtained by the bank serving as Administrative Agent or any of its Affiliates in any capacity. The Administrative Agent shall not be liable for any action taken or not taken by it with the consent or at the request of the Required Banks (or such other number or percentage of the Banks as shall be necessary under the circumstances as provided in Section 10), or in the absence of its own gross negligence or willful misconduct. The Administrative Agent shall be deemed not to have knowledge of any Reimbursement Event of Default unless and until written notice thereof is given to the Administrative Agent by the Company or a Bank, and the Administrative Agent shall not be responsible for or have any duty to ascertain or inquire into (i) any statement, warranty or representation made in or in connection with this Agreement, (ii) the contents of any certificate, report or other document delivered hereunder or in connection with this Agreement, (iii) the performance or observance of any of the covenants, agreements or other terms or conditions set forth in this Agreement, (iv) the validity, enforceability, effectiveness or genuineness of this Agreement or any other agreement, instrument or document, or (v) the satisfaction of any condition set forth in Section 3 or elsewhere in this Agreement, other than to confirm receipt of items expressly required to be delivered to the Administrative Agent.

(iii) The Administrative Agent shall be entitled to rely upon, and shall not incur any liability for relying upon, any notice, request, certificate, consent, statement, instrument, document or other writing reasonably believed by it to be genuine and correct and to have been signed or sent by the proper Person. The Administrative Agent also may rely upon any statement made to it orally or by telephone (except when a writing is expressly required) and reasonably believed by it to be made by the proper Person, and shall not incur any liability for relying thereon.

(iv) The Administrative Agent may perform any and all its duties and exercise its rights and powers hereunder by or through any one or more sub-agents appointed by the Administrative Agent in the exercise of reasonable care.

(v) Subject to the appointment and acceptance of a successor Administrative Agent as provided in this paragraph, the Administrative Agent may resign at any time by notifying the Banks and the Company. Upon any such resignation, the Required Banks shall have the right, with the prior written approval of the Company (which approval will not be unreasonably withheld or delayed and which shall be required only so long as no Reimbursement Event of Default shall be continuing), to appoint a successor. If no successor shall have been so appointed by the Required Banks and shall have accepted such appointment within 30 days after the retiring Administrative Agent gives notice of its resignation, then the retiring Administrative Agent may, on behalf of the Banks, appoint a successor Administrative Agent which shall be a commercial bank having capital and retained earnings of at least $100,000,000 or an Affiliate of any such commercial bank. Upon the acceptance of its appointment as Administrative Agent

hereunder by a successor, such successor shall succeed to and become vested with all the rights, powers, privileges and duties of the retiring Administrative Agent, and the retiring Administrative Agent shall be discharged from its duties and obligations hereunder. The fees payable by the Company to a successor Administrative Agent shall be the same as those payable to its predecessor unless otherwise agreed between the Company and such successor. After the Administrative Agent's resignation hereunder, the provisions of this Section 20 and Sections 19 and 21 shall continue in effect for the benefit of such retiring Administrative Agent, its sub agents and their respective Affiliates in respect of any actions taken or omitted to be taken by any of them while it was acting as Administrative Agent.

(vi) Each Bank acknowledges that it has, independently and without reliance upon the Administrative Agent or any other Bank and based on such documents and information as it has deemed appropriate, made its own credit analysis and decision to enter into this Agreement. Each Bank also acknowledges that it will, independently and without reliance upon the Administrative Agent or any other Bank and based on such documents and information as it shall from time to time deem appropriate, continue to make its own decisions in taking or not taking action under or based upon this Agreement or related agreement or any document furnished hereunder.

(b) The Administrative Agent and its Affiliates may accept deposits from, make loans or otherwise extend credit to, and generally engage in any kind of business with, the Company, the Equity Participant and their respective Subsidiaries and Affiliates and receive payment on such loans or extensions of credit and otherwise act with respect thereto freely and without accountability in the same manner as if this Agreement and the transactions contemplated hereby were not in effect.

(c) The Administrative Agent may consult with legal counsel (who may be counsel for the Company), independent public accountants and other experts as it may select and shall not be liable for any action taken or omitted to be taken by it in good faith in accordance with the advice of such counsel, accountants or experts.

(d) It is understood that the Issuing Bank will exercise and give the same care and attention to the Letter of Credit as it gives to its other letters of credit and loans for its own account and that the Issuing Bank shall have no obligation to the Company or any other Bank and no duty or responsibility with respect to this Agreement or the Letter of Credit, except as expressly provided herein and in the Letter of Credit. Without limiting the generality of the foregoing, the Issuing Bank shall not be required to take any action with respect to any Reimbursement Default, except as expressly provided in Section 9 hereof. The Issuing Bank shall not be liable for any action taken or not taken at the request or with the approval of the Required Banks (or all the Banks, as applicable) or for the performance or non-performance of the obligations of any other party under this Agreement or any Transaction Document or Financing Document or any other document contemplated thereby. It is further understood that: (i) except as expressly limited by the provisions of this Agreement, the Issuing Bank retains the sole right to exercise its rights and enforce the obligations of the Company under this Agreement, and the Issuing Bank may use its sole discretion with respect to exercising or refraining from exercising any rights or taking or refraining from taking any actions which may be vested in it or which it may be entitled to take or assert under this Agreement or any of the Transaction

Documents or Financing Documents (including, without limitation, the giving of any notice to any Person of any Reimbursement Event of Default under this Agreement except as provided in Section 9); and (ii) the Issuing Bank shall not, in the absence of gross negligence or willful misconduct, be under any liability to any other Bank with respect to anything which the Issuing Bank may do or refrain from doing in the exercise of its best judgment or which it may deem to be necessary or desirable. Neither the Administrative Agent nor the Issuing Bank shall incur any liability by acting in reliance upon any written communication or any telephone conversation which it reasonably believes to be genuine and correct or to have been signed, sent or made by the proper Person. Neither the Administrative Agent nor the Issuing Bank shall have any obligation to make any claim on, or assert any lien upon, or assert any setoff against, any property held by it and, if it elects to do so, it may in its discretion apply the same against indebtedness of the Company other than the Company's obligations under this Agreement; *provided* that, to the extent any funds received pursuant to any of the foregoing are applied to the obligations of the Company under Section 2(a) or 2(b) hereof, each Bank shall be entitled to receive its pro rata share thereof in accordance with Section 14(b) above. Any such setoff or other action in respect of any reimbursement obligation of the Company set forth in Section 2(a) will be subject to Section 13.

Section 21. *Indemnification*. (a) To the fullest extent permitted by law, the Company shall indemnify and hold harmless the Administrative Agent, the Issuing Bank, each Bank, their respective affiliates and correspondents and each of their respective directors, officers, employees and agents (each such party, an "**Indemnified Party**") from and against any and all claims, suits, judgments, costs, losses, fines, penalties, damages, liabilities, and expenses, including expert witness fees and reasonable legal fees, charges and disbursements of any counsel (including in-house counsel fees and allocated costs) for any Indemnified Party ("**Costs**") (except to the extent any such Costs are expressly stated in this Agreement to be payable by the Indemnified Party or to the extent expressly limited pursuant to Sections 2(d), 2(e), 2(f), 7(e), 18(a) and 19), arising out of, in connection with, or as a result of: (i) the Letter of Credit or any pre-advice of its issuance; (ii) any action or proceeding arising out of or in connection with the Letter of Credit or this Agreement (whether administrative, judicial or in connection with arbitration), including any action or proceeding to compel or restrain any presentation or payment under the Letter of Credit, or for the wrongful dishonor of or honoring a presentation under the Letter of Credit; (iii) any Instruction that is unauthorized and that is (x) received pursuant to the express terms of the Letter of Credit or (y) any other Instruction regarding the Letter of Credit or error in computer transmission that in either case the Indemnified Party reasonably believed to be authorized; (iv) any third party seeking to enforce the rights of an applicant, beneficiary, nominated person, transferee or assignee of proceeds of the Letter of Credit; (v) the fraud, forgery or illegal action of parties other than the Indemnified Party (including, for the avoidance of doubt, any fraud, forgery or illegal action by any party in connection with any transfer of the Letter of Credit); (vi) the enforcement against the Company of this Agreement or any rights or remedies under or in connection with this Agreement or the Letter of Credit; (vii) the Administrative Agent's or the Issuing Bank honoring any presentation upon or during the continuance of any Reimbursement Event of Default or for which the Company is unable or unwilling to make any payment to the Administrative Agent, the Issuing Bank or any Bank as required under this Agreement; (viii) the acts or omissions, whether rightful or wrongful, of any present or future de jure or de facto governmental or regulatory authority or cause or event beyond the control of such Indemnified Party; in each case, including that

resulting from the Administrative Agent's or the Issuing Bank's own negligence, provided, however, that such indemnity shall not be available to any Person claiming indemnification under (i) through (viii) above to the extent that such Costs are found in a final, non-appealable judgment by a court of competent jurisdiction to have resulted directly from the gross negligence or willful misconduct of the Indemnified Party claiming indemnity, in which case any fees or expenses previously paid or advanced by the Company to such Indemnified Party in respect of such indemnified obligation (if any) will be returned by such Indemnified Party. Without limitation of the foregoing, the Company shall not be required to indemnify the Issuing Bank or its Related Parties pursuant to this Section for any Costs to the extent solely caused by (i) the Issuing Bank's willful misconduct or gross negligence in determining whether documents presented under the Letter of Credit comply with the terms of the Letter of Credit or (ii) its willful failure to make lawful payment under the Letter of Credit after presentation to it by the beneficiary of the Letter of Credit of documents strictly complying with the terms and conditions of the Letter of Credit. If and to the extent that the obligations of Company under this paragraph are unenforceable for any reason, Company shall make the maximum contribution to the Costs permissible under applicable law.

(b) To the extent permitted by applicable law, the foregoing provisions shall supersede any indemnity provisions set forth in Section 8.01(b) of the ISP.

(c) To the extent that the Administrative Agent or the Issuing Bank is not reimbursed and indemnified by the Company under this Agreement, each Bank will reimburse and indemnify the Administrative Agent and the Issuing Bank on demand for and against such Bank's Participation Percentage of any and all claims, demands, liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements (including fees and disbursements of counsel) of any kind or nature whatsoever which may be imposed on, incurred by, or asserted against the Administrative Agent or the Issuing Bank in any way relating to or arising out of this Agreement, the Fee Letter, the Letter of Credit, or any of the Transaction Documents or Financing Documents or any action taken or omitted to be taken by the Administrative Agent or the Issuing Bank hereunder or thereunder, or the transactions contemplated hereby and thereby or the enforcement of any of the terms hereof and thereof; *provided* that such Bank shall not be liable for any portion of such claims, demands, liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, out-of-pocket expenses or disbursements resulting from the gross negligence or willful misconduct of the Administrative Agent or the Issuing Bank or which are expressly excluded from the indemnification by the Company by the proviso to the first sentence of Section 21(a), or by the second sentence of Section 21(a) of this Agreement. Each Bank's obligations under this Section 21(c) shall survive the termination of this Agreement and the Letter of Credit. If the Administrative Agent or the Issuing Bank is reimbursed by the Company for any amounts previously received from any Bank pursuant to this Section 21(c), it will promptly pay to such Bank its proportionate share of any amounts so received.

Section 22. *Confidentiality*. (a) The Administrative Agent and each Bank agree (on behalf of themselves and each of their Affiliates, directors, officers, employees and representatives) to take normal and reasonable precautions and exercise due care to maintain the confidentiality of all non-public information provided to them by the Company or any Subsidiary of the Company in connection with this Agreement and neither the Administrative Agent, any

Bank nor any of their Affiliates, directors, officers, employees and representatives shall use any such information for any purpose or in any manner other than pursuant to the terms contemplated by this Agreement, except to the extent such information (a) was or becomes generally available to the public other than as a result of a disclosure by the Administrative Agent or any Bank, or (b) was or becomes available on a non-confidential basis from a source other than the Company, provided that such source is not bound by a confidentiality agreement with the Company known to the Administrative Agent or affected Bank after reasonable inquiry; provided that nothing herein shall limit the disclosure of any such information (i) to the extent required by statute, rule, regulation or judicial process; (ii) to counsel for the Administrative Agent or any Bank; (iii) to bank examiners, auditors or accountants, on a confidential basis; (iv) to the Administrative Agent or any other Bank; (v) by the Administrative Agent or any Bank to an Affiliate thereof who is bound by this Section 22; provided that any such information delivered to an Affiliate shall be for the purposes related to the extension of credit represented by this Agreement and the administration and enforcement thereof and for no other purpose; (vi) in connection with any litigation relating to enforcement of this Agreement or (vii) to any assignee or participant (or prospective assignee or participant) so long as such assignee or participant (or prospective assignee or participant) first enters into a confidentiality agreement with the respective Bank, which confidentiality agreement shall contain terms substantially similar to the terms set forth in this Section 22. Each Bank and the Administrative Agent agree, unless specifically prohibited by applicable law or court order, to notify the Company of any request for disclosure of any such non-public information (x) by any governmental authority or representative thereof (other than any such request in connection with an examination of the financial condition of the Company by such governmental authority) or (y) pursuant to legal process. The obligations under this Section 22 shall survive for two (2) years after termination of this Agreement.

(b) This Agreement is intended to provide express authorization to each of the Banks and their Affiliates (and each employee, representative, or other agent of each Bank and its respective Affiliates) to disclose to any and all Persons, without limitation of any kind, the “tax treatment” and “tax structure” (in each case, within the meaning of Treasury Regulation Section 1.6011-4) of the transactions contemplated hereby and all materials of any kind (including opinions or other tax analyses) that are provided to the Banks or any of their Affiliates (and any such employees, representatives or other agents) relating to such tax treatment and structure; provided, that, with respect to any document or similar item that in either case contains information concerning the tax treatment or tax structure of the transactions contemplated hereby as well as other information, this authorization shall only apply to such portions of the documents or similar item that relate to the tax treatment or tax structure of the transactions contemplated hereby.

Section 23. *Severability*. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

Section 24. *Governing Law; Consent to Jurisdiction*. (a) This Agreement shall be governed by, and construed in accordance with, the laws of the State of New York.

(b) Each party hereto submits to the nonexclusive jurisdiction of the Supreme Court of the State of New York sitting in New York County and of the United States District Court of the Southern District of New York, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or for recognition or enforcement of any judgment, and each party hereto hereby agrees, to the fullest extent permitted by law, that all claims in respect of any such action or proceeding may be heard and determined in such New York State or, to the extent permitted by law, in such Federal court. Nothing in this Agreement shall affect any right that any party hereto may otherwise have to bring action or proceeding relating to this Agreement in the courts of any jurisdiction.

Section 25. *Headings*. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 26. *Counterparts; Integration*. This Agreement may be signed in any number of counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument. This Agreement, the Fee Letter, that certain Commitment Agreement dated as of March 17, 2010 between JPMorgan, J.P. Morgan Securities Inc., Union Bank, N.A., and the Company, that certain Letter Agreement between the Issuing Bank and the Company dated as of April 16, 2010 constitute the entire agreement and understanding among the parties hereto and, subject to Section 3(c), supersede any and all prior agreements and understandings, oral or written, relating to the subject matter hereof.

Section 27. *WAIVER OF JURY TRIAL*. TO THE EXTENT ALLOWED BY LAW, EACH OF THE COMPANY, THE BANKS AND THE ADMINISTRATIVE AGENT HEREBY IRREVOCABLY WAIVES ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY.

Section 28. *No Advisory or Fiduciary Responsibility*. In connection with all aspects of each transaction contemplated hereby (including in connection with any amendment, waiver or other modification hereof or any syndication of the credit facility provided hereunder), the Company acknowledges and agrees that: (i) (A) the arranging and other services regarding this Agreement provided by the Administrative Agent are arm's-length commercial transactions between the Company and its Affiliates, on the one hand, and the Administrative Agent and its Affiliates, on the other hand, (B) it has consulted its own legal, accounting, regulatory and tax advisors to the extent it has deemed appropriate, and (C) it is capable of evaluating, and understands and accepts, the terms, risks and conditions of the transactions contemplated hereby; (ii) (A) the Administrative Agent and the Company each is and has been acting solely as a principal and, except as expressly agreed in writing by the relevant parties, has not been, is not, and will not be acting as an advisor, agent or fiduciary for any other party hereto, any Affiliates of any other party hereto, or any other Person and (B) none of the Administrative Agent or the Company has any obligation to each other or to their respective Affiliates with respect to the transactions contemplated hereby except those obligations expressly set forth herein; and (iii) the Administrative Agent and its Affiliates may be engaged in a broad range of transactions that involve interests that differ from those of the Company and its Affiliates, and the Administrative Agent has no obligation to disclose any of such interests to the Company or its Affiliates. To the

fullest extent permitted by law, the Administrative Agent and the Company hereby waive and release any claims that they may have against each other with respect to any breach or alleged breach of agency or fiduciary duty in connection with any aspect of any transaction contemplated hereby. Each of the Administrative Agent and the Banks acknowledge and agree that it has consulted its own legal, accounting, regulatory and tax advisors to the extent it has deemed appropriate.

Section 29. *Waiver of Damages*. To the extent allowed by law, no party hereto shall have any liability with respect to, and each party hereto hereby waives, releases and agrees not to sue for, any special, indirect, consequential or punitive damages or losses suffered by such party in connection with, arising out of, or in any way related to this Agreement, the Letter of Credit or the transactions contemplated hereby or thereby regardless of whether such party shall have been advised of the possibility of such damages or losses or of the form of action in which such damages or losses may be claimed.

Section 30. *Government Regulations*. The Company agrees to provide documentary and other evidence of the Company's identity as may be requested by any Bank at any time to enable such Bank to verify the Company's identity or to comply with any applicable law or regulation, including, without limitation, Section 326 of the USA Patriot Act of 2001, 31 U.S.C. Section 5318.

Signature Pages Follow

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By: /s/ James R. Hatfield
Name: James R. Hatfield
Title: Senior Vice President and Chief Financial Officer

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent, Issuing Bank and as a Bank

By: /s/ Nancy R. Barwig
Name: Nancy R. Barwig
Title: Vice President

UNION BANK, N.A., as a Bank

By: /s/ Pascal Uttinger
Name: Pascal Uttinger
Title: Vice President

SCHEDULE I

The "**Letter of Credit Commission Rate**" and the "**Base Rate Margin**" for any day is the rate set forth below (in basis points per annum) under the column corresponding to the Status that exists on such day:

Status	Level I	Level II	Level III	Level IV	Level V
Base Rate Margin	100.0	150.0	175.0	200.0	250.0
Letter of Credit Commission Rate	200.0	250.0	275.0	300.0	350.0

For purposes of this Schedule, the following terms have the following meanings:

"**Level I Status**" exists at any date if, at such date, the higher of the two Ratings is:

A- or higher by S&P or A3 or higher by Moody's.

"**Level II Status**" exists at any date if, at such date, (i) Level I Status does not exist and (ii) the higher of the two Ratings is:

BBB+ or higher by S&P or Baa1 or higher by Moody's.

"**Level III Status**" exists at any date if, at such date, (i) neither Level I Status nor Level II Status exists and (ii) the higher of the two Ratings is:

BBB or higher by S&P or Baa2 or higher by Moody's.

"**Level IV Status**" exists at any date if, at such date, (i) none of Level I Status, Level II Status and Level III Status exists and (ii) the higher of the two Ratings is:

BBB- or higher by S&P or Baa3 or higher by Moody's.

"**Level V Status**" exists at any date if, at such date, no other Status exists.

"**Moody's**" means Moody's Investors Service, Inc., and any successor thereto.

"**Rating Agencies**" means Moody's and S&P.

"**Ratings**" means the credit ratings assigned to the senior unsecured long-term debt securities of the Company without third-party credit enhancement by the Rating Agencies. If there is no rating assigned to debt securities, the corporate credit rating will be used; and if Moody's or S&P shall not have in effect any rating assigned to senior unsecured long-term debt securities of the Company or corporate credit rating (other than by circumstances referred to in the last sentence of this definition), then such Rating Agency shall be deemed to have established

a Rating in Level V. Any rating assigned to any other debt security of the Company shall be disregarded. The rating in effect at any date is that in effect at the close of business on such date. In the case of split ratings from S&P or Moody's, the rating to be used to determine which pricing level applies is the higher of the two (e.g., BBB+/Baa2 results in Level II Status); provided that if the split is more than one full rating category, the rating category next below that of the higher of the two rating categories will be used (e.g., BBB+/Baa3 results in Level III Status, and A-/Baa3 results in Level II Status). If the rating system of Moody's or S&P shall change, or if either such Rating Agency shall cease to be in the business of rating corporate debt obligations, the Company, the Administrative Agent and the Banks shall negotiate in good faith to amend this definition to reflect such changed rating system or the unavailability of ratings from such Rating Agency and, pending the effectiveness of any such amendment, the Letter of Credit Commission Rate and the Base Rate Margin shall be determined by reference to the Rating most recently in effect prior to such change or cessation.

"**S&P**" means Standard & Poor's Financial Services LLC, a division of The McGraw-Hill Companies, Inc., and any successor thereto.

"**Status**" refers to the determination of which of Level I Status, Level II Status, Level III Status, Level IV Status or Level V Status exists at any date.

SCHEDULE II

Bank	Participation Percentage	Participation Amount
JPMorgan Chase Bank, N.A.	51.46682890154%	$ 14,060,240.49
Union Bank, N.A.	48.53317109846%	$ 13,258,793.51

EXHIBIT A

AMENDED AND RESTATED
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. P-010151
(formerly numbered as S-1001)

Originally Issued August 18, 1986
Amended and Restated
April 16, 2010

Security Pacific Capital Leasing Corporation
555 California Street, 4th Floor
Mail Code: CA5-705-04-01
San Francisco, California 94104

Attention: Anita Garfagnoli

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "**Company**"), in your favor, our Irrevocable Transferable Letter of Credit No. P-010151 (formerly numbered as S-1001) (the "**Letter of Credit**"), in a maximum amount at any date (the "**Maximum Credit Amount**") equal to the amount shown opposite the period including such date in the Table of Maximum Credit Amounts attached hereto as Schedule II-A, effective immediately and expiring at 5:00 p.m. (New York City time) on the Termination Date. Capitalized terms used herein and in Schedules II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "**Facility Lease**") as amended and in effect on the date hereof, between the Company and U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston), as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "**Date of Drawing**") in the Table of Maximum Drawing Amounts attached hereto as Schedule II-B as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next paragraph, are hereinafter referred to collectively as the "**Maximum Drawing Amounts**" and individually as the "**Maximum Drawing Amount**". A drawing in respect of a payment hereunder honored by us shall not exceed the lesser of the Maximum Drawing Amount applicable on the Date of Drawing and the Maximum Credit Amount applicable on the Date of Drawing. All payments hereunder shall be made from our own general funds.

The Maximum Drawing Amounts shall be modified from time to time as follows:

(a) upon payment by the Issuing Bank of each drawing under the Letter of Credit, the Maximum Drawing Amounts applicable to each Date of Drawing subsequent to such payment shall be automatically reduced by an amount equal to the amount of the drawing so paid and shall not be reinstated; and

(b) if adjustments are made to Modified Special Casualty Values, corresponding adjustments shall be made to the Maximum Drawing Amounts shown in Schedule II-B, (as theretofore reduced pursuant to clause (a) above), *provided* that if any such adjustment of Modified Special Casualty Values would cause the Maximum Drawing Amount for any period to exceed the Maximum Credit Amount for such period, (minus, the amount of any drawing theretofore honored by us hereunder), such Maximum Credit Amount (as so reduced) shall apply for such period and *provided further* that adjustments pursuant to this clause (b) shall be effective automatically upon receipt by us of a notice from you in the form of Exhibit 1 hereto.

Upon receipt of a notice in the form of Exhibit 1 hereto, we will promptly issue an amendment to this irrevocable transferable letter of credit containing a revised Schedule II-B reflecting the adjustments contained in such notice.

Funds under this Letter of Credit are available to you against presentation on or prior to the Termination Date of your drawing in the form of a completed certificate signed by you in the form of Exhibit 2 attached hereto. Such certificate shall be dated the date of its presentation and shall be presented (x) by facsimile (at facsimile number (312) 233-2266 or alternately to (312) 954-2458), Attention: Manager, without further need of documentation, including the original of this Letter of Credit, or (y) at our Chicago office specified below, in each case, it being understood that each certificate so submitted is to be the sole operative instrument of drawing. You shall use your best efforts to give telephonic notice of a drawing to the Issuing Bank at its Standby Service Unit, (at: (312) 954-5973 or alternately to 1-800-634-1969, Option 1) on the day of such drawing (but such notice shall not be a condition to drawing hereunder and you shall have no liability for not doing so). If we receive such certificate as provided herein, in strict conformity with the terms and conditions of this Letter of Credit, prior to 10:00 a.m. (New York City time) on any Business Day, (notwithstanding any provision of Rule 5.01 of the International Standby Practices, ICC Publication No. 590 (the "**ISP98**") to the contrary, which provisions of the ISP98 are hereby expressly waived), we will honor the drawing on the same Business Day. If we receive such certificate as provided herein on or after 10:00 a.m. and prior to 5:00 p.m. (New York City time) on any Business Day, all in strict conformity with the terms and conditions of this Letter of Credit, we will honor the drawing on the next Business Day. Payment under this Letter of Credit will be made by wire transfer of federal funds to your account with any bank located in the United States of America or by deposit of immediately available funds into a designated account that you maintain with us.

Notwithstanding any provision of Section 5-108(b) of the New York Uniform Commercial Code (the "**NY UCC**") or Rule 5.01 of the ISP98 to the contrary, which provisions are hereby expressly waived, if the presentation of such certificate is not in strict conformity with the terms and conditions of this Letter of Credit, we will give you prompt notice prior to the time we would have been obliged to make payment as set forth in the preceding paragraph by

facsimile transmission addressed to you at the fax number set forth in the next succeeding paragraph, effective upon confirmation, that we have refused such non-conforming certificate, and stating all discrepancies in respect of which the Issuing Bank refuses such non-conforming certificate. If you correct such non-conforming demand by presentation of the certificate corrected to be in strict conformity with the terms and conditions of the Letter of Credit, then we will honor the drawing and make payment in accordance with the terms provided herein based upon the time such corrected certificate is presented, *provided* that you may make only one such corrected demand with respect to any such non-conforming demand, and *provided further* that any such correction and presentation of such conforming demand is effected on or prior to the Stated Termination Date, and *provided further* that for purposes of determining whether such certificate has been timely presented, the corrected certificate shall be deemed to have been presented on the date the non-conforming certificate was presented.

Notwithstanding any other provision of this Letter of Credit, we shall have the right, upon the occurrence of any of the events listed in Schedule III hereto, to terminate this Letter of Credit by delivering to you a written notice in the form of Exhibit 4 hereto indicating the date of such termination (the "**Date of Early Termination**"), *provided* that on or before the Date of Early Termination you will have the right to draw once an amount not in excess of the lesser of the Maximum Credit Amount and the Maximum Drawing Amount in accordance with the procedures described herein. The written notice referred to in the preceding sentence shall be given by facsimile transmission addressed to you at Security Pacific Capital Leasing Corporation, 555 California Street, 4th Floor, Mail Code: CA5-705-04-01, San Francisco, California 94104; Attention: Anita Garfagnoli; Fax: 415-765-7373 (or to such other address or facsimile number designated by you by written notice delivered to us at least 15 days prior to the notice of early termination) and shall be effective upon receipt of the appropriate confirmation of the facsimile transmission. We will also forward a copy of such notice by overnight delivery service to the address set forth above. The Date of Early Termination specified in such written notice shall be:

(a) in the case of events specified in paragraphs A and G of Schedule III, not earlier than ten days after such notice is given, and

(b) in the case of all other events specified in Schedule III, not earlier than 30 days after such notice is given.

Upon the Termination Date this Letter of Credit shall automatically terminate and be delivered to the Issuing Bank for cancellation. Failure to deliver said Letter of Credit will have no effect on the Termination Date, and the Letter of Credit will still be considered terminated.

Notwithstanding the provisions of Section 5-112(b)(2) of the NY UCC that permit the Issuing Bank to refuse to recognize or carry out a transfer of this Letter of Credit if the transferee has failed to comply with any other requirement relating to transfer imposed by the Issuing Bank which is within the standard practice referred to in Section 5-108(e) of the NY UCC or is otherwise reasonable under the circumstances, which provisions are hereby expressly waived, this Letter of Credit may be transferred in its entirety more than once, but in each case only to the successor Equity Participant under the Trust Agreement dated as of August 1, 1986 between yourself and U.S. Bank National Association (as successor to State Street Bank and Trust

Company, as successor to The First National Bank of Boston). Any transfer request must be effected by presenting to the Issuing Bank the attached form of Exhibit 3 hereto signed by the transferor and by the transferee accompanied by the original of this Letter of Credit and any amendments thereto (which presentation of an appropriately completed Exhibit 3 shall be conclusive evidence of such transferee's authority without any inquiry by us into the terms of the Trust Agreement). Upon the Issuing Bank's endorsement of such transfer, the transferee instead of the transferor shall, without necessity of further action, be entitled to all the benefits of and rights under this Letter of Credit in the transferor's place.

Notwithstanding any provision of Rule 3.12 of the ISP98 to the contrary, which provisions are hereby expressly waived, upon the Issuing Bank's receipt of its standard certificate duly executed by you certifying that the original of this Letter of Credit has been lost, destroyed or mutilated, the Issuing Bank shall provide a true copy of original (which copy shall be marked as such) of this Letter of Credit to you without affecting the Company's obligations to the Issuing Bank to reimburse. Upon delivery of such copy, any requirement that the original be presented hereunder shall be deemed to be a reference to such copy.

Except as expressly stated herein, this Letter of Credit is governed by, and construed in accordance with the ISP98. As to matters not governed by the ISP98, this Letter of Credit shall be governed by and construed in accordance with the laws of the State of New York, including without limitation the NY UCC as in effect in the State of New York, without regard to principles of conflict of laws (other than Sections 5.1401 and 5.1402 of the General Obligations Law of the State of New York).

Communications with respect to this Letter of Credit shall be in writing, specifically referring to the number of this Letter of Credit, and addressed and presented to the Issuing Bank at JPMorgan Chase Bank, N.A., 300 South Riverside Plaza, Mail Code IL1-0236, Chicago, Il 60606-0236, Attention: Standby Letter of Credit Unit. For telephone assistance, please contact the Standby Client Service Unit at 1-800-634-1969, select Option 1, and have this Letter of Credit number available.

By your acceptance of this Letter of Credit, we hereby notify you of our agreement to the terms and conditions of Section 13 of the Reimbursement Agreement.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein, except only Schedules I, II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto and the notices referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except as set forth above.

This Letter of Credit No. P-010151 (formerly numbered as S-1001) amends and restates our Letter of Credit No. S-1001 dated as of August 15, 1986, as heretofore amended.

JPMORGAN CHASE BANK, N.A.

By: _____
Name:
Title:

EXHIBIT 1
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236

Attn: Standby Letter of Credit Unit

Dear Sirs:

Reference is made to that certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010151 (formerly numbered as S-1001) dated April 16, 2010 (the "**Letter of Credit**"), which has been established by you in favor of Security Pacific Capital Leasing Corporation (the "**Equity Participant**").

The undersigned, a duly authorized representative of the Equity Participant, hereby certifies that Modified Special Casualty Values have been adjusted and the amounts shown on Schedule II-B to the Letter of Credit should be modified, in accordance with the terms of clauses (a) and (b) of the third paragraph of the Letter of Credit, to the amounts shown in Appendix A hereto.

We request that you amend the Letter of Credit to replace the current Schedule II-B to the Letter of Credit with the revised Schedule II-B attached hereto. All other terms and conditions as stated in the Letter of Credit will remain unchanged. Except as otherwise set forth herein, the Letter of Credit shall remain effective and in full force.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

_____
[Name of Equity Participant**]**

_____
[Name and Title of Authorized

_____
Representative of Equity Participant**]**

EXHIBIT 2
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

CERTIFICATE

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236
Attn: Standby Letter of Credit Unit
Facsimile number (312) 233-2266
Alternately to (312) 954-2458

The undersigned, a duly authorized representative of Security Pacific Capital Leasing Corporation (the "**Equity Participant**"), as beneficiary under that certain amended and restated irrevocable transferable Letter of Credit No. P-010151 (formerly numbered as S-1001) dated April 16, 2010, established by JPMorgan Chase Bank, N.A. (the "**Issuing Bank**") and issued pursuant to that certain Reimbursement Agreement dated as of April 16, 2010 between Arizona Public Service Company (the "**Company**"), the Issuing Bank and the other Banks named therein, hereby certifies as follows:

1. We hereby demand payment in the amount of $_____.

2. An Event of Default under the Facility Lease has occurred and is continuing.

3. The amount demanded hereby does not exceed the Maximum Drawing Amount available under the Letter of Credit on the date hereof, as determined in accordance with the terms of the Letter of Credit.

4. Payment by the Issuing Bank pursuant to this drawing shall be made to _____, ABA Number _____, Account Number _____, Attention: _____, Re: _____.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed this Certificate as of _____, 20_____.

_____
[Name of Equity Participant**]**

[Name and Title of Authorized
Representative of Equity Participant**]**

EXHIBIT 3
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

REQUEST FOR TRANSFER

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236

[Date**]**

Attn: Standby Letter of Credit Unit

Re: JPMorgan Chase Bank, N.A. Irrevocable Transferable Letter of Credit No. P-010151 (formerly numbered as S-1001) dated April 16, 2010.

We, the undersigned "Transferor", hereby irrevocably transfer all of our rights to draw under the above referenced Letter of Credit ("Credit") in its entirety to:

NAME OF TRANSFEREE _____
(Print Name and complete address of the Transferee) "Transferee"

ADDRESS OF TRANSFEREE _____

_____

CITY, STATE/COUNTRY ZIP _____

In accordance with ISP98 (as defined in the Credit), Rule 6, regarding transfer of drawing rights, all rights of the undersigned Transferor in such Credit are transferred to the Transferee, who shall have the sole rights as beneficiary thereof, including sole rights relating to any amendments whether increases or extensions or other amendments and whether now existing or hereafter made. All amendments are to be advised directly to the Transferee without necessity of any consent of or notice to the undersigned Transferor.

The original Credit, including amendments to this date, is attached and the undersigned Transferor requests that you endorse an acknowledgment of this transfer on the reverse thereof. The undersigned Transferor requests that you notify the Transferee of this Credit in such form and manner as you deem appropriate, and the terms and conditions of the Credit as transferred. The undersigned Transferor acknowledges that you incur no obligation to process the transfer requested hereunder if the transfer is to a prohibited person named by the United States Department of Treasury's Office of Foreign Assets Control Regulations.

The Transferor and the Transferee hereby request that you advise the Transferee of the terms and conditions of this transferred Credit and these instructions.

In the event that the authorized signatory for either the Transferor or the Transferee is a financial institution, a corporation or a partnership composed of financial institutions or corporations, a secretary or incumbency certificate certifying that such signatory is duly empowered to act in the name and on behalf of such Transferor or Transferee, as applicable, must accompany this

Request for Transfer, and, in such case, the requirement that such signatory's signature be guaranteed shall be deemed to be waived.

Payment of transfer fee of U.S. $3,500 is for the account of the Company (as defined in the Credit) who agrees to pay you on demand any expense or cost you may incur in connection with the transfer. Receipt of such transfer fee shall not constitute consent to effect the transfer of the Credit on terms other than as expressly set forth in the Credit and this Request for Transfer.

Transferor represents and warrants to you that (i) our execution, delivery, and performance of this request for transfer (a) are within our powers, (b) have been duly authorized, (c) constitute our legal, valid, binding and enforceable obligation, (d) do not contravene any charter provision, by-law, resolution, contract, or other undertaking binding on or affecting us or any of our properties, (e) to the best of Transferor's knowledge, such transfer does not require any notice, filing or other action to, with, or by any governmental authority, (f) the enclosed Credit is original and complete, (g) there is no outstanding demand or request for payment or transfer under the Credit affecting the rights to be transferred which remains outstanding as of the date hereof, (h) in the event that the Transferee's signature is not guaranteed, to the best of Transferor's knowledge, the Transferee is a financial institution, a corporation or a partnership composed of financial institutions or corporations and (i) to the best of Transferor's knowledge, based on information provided by the Transferee, the Transferee's name and address are correct and complete and the Transferee's use of the Credit as transferred and the transactions underlying the Credit and the requested transfer do not violate any applicable United States or other law, rule or regulation.

The effective date of the transfer shall be the date hereafter on which you effect the requested transfer by acknowledging and endorsing this request and giving notice thereof to Transferee.

WE WAIVE ANY RIGHT TO TRIAL BY JURY THAT WE MAY HAVE IN ANY ACTION OR PROCEEDING RELATING TO OR ARISING OUT OF THIS TRANSFER.

This request is made subject to ISP98 and is subject to and shall be governed by the laws of the State of New York, without regard to principles of conflict of laws.

Sincerely yours,

_____
(Print Name of Transferor)

_____
(Transferor's Authorized Signature)

_____
(Print Authorized Signers Name and Title)

SIGNATURE GUARANTEED

Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement. We attest that the individual, company or entity has been identified by us in compliance with USA PATRIOT Act procedures of our bank.

_____
(Print Name of Bank)

_____
(Address of Bank)

_____
(City, State, Zip Code)

_____
(Print Name and Title of Authorized Signer)

_____
(Authorized Signature)

_____
(Telephone Number)

_____
(Date)

(Telephone Number/Fax Number)

Acknowledged:

(Print Name of Transferee)

(Transferee's Authorized Signature)

(Print Authorized Signers Name and Title)

(Telephone Number/Fax Number)

Acknowledged as of _____, 20_____:

JPMorgan Chase Bank, N.A.

By: _____
Name:
Title:

SIGNATURE GUARANTEED

Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement. We attest that the individual, company or entity has been identified by us in compliance with USA PATRIOT Act procedures of our bank.

(Print Name of Bank)

(Address of Bank)

(City, State, Zip Code)

(Print Name and Title of Authorized Signer)

(Authorized Signature)

(Telephone Number)

(Date)

EXHIBIT 4
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

NOTICE OF TERMINATION

Date: _____ __, 20__

Security Pacific Capital Leasing Corporation
555 California Street, 4th Floor
Mail Code: CA5-705-04-01
San Francisco, California 94104

Attention: Anita Garfagnoli

Dear Sir:

Reference is made to that certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010151 (formerly numbered as S-1001) dated April 16, 2010, which has been established by us in your favor.

We hereby give notice to you that the above referenced Letter of Credit will be terminated in accordance with its terms on _____ _____, 20_____, pursuant to the occurrence of one or more of the events described in Schedule III to the Letter of Credit as follows:

[Insert the description of the event(s) of default**]**

Very truly yours,

JPMORGAN CHASE BANK, N.A.

By: _____
Name:
Title:

SCHEDULE I
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

The following terms have the following meanings for purposes of the Letter of Credit and the Schedules and Exhibits thereto. Terms defined in the Letter of Credit have the meanings given to them therein. Terms defined by reference to the Facility Lease have the meanings assigned to them therein from time to time.

"**Administrative Agent**" means JPMorgan, in its capacity as administrative agent for the Banks under the Reimbursement Agreement, and its successors in such capacity.

"**Applicable Law**" has the meaning assigned to it in the Facility Lease.

"**Bank**" means (i) each bank or financial institution listed on the signature pages of the Reimbursement Agreement, each Assignee that becomes a Bank pursuant to Section 15(a) of the Reimbursement Agreement, and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"**Business Day**" means any day except (i) a Saturday or Sunday, (ii) any other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close, or (iii) a day on which payments in respect of the Letter of Credit cannot be funded via wire through the Federal Reserve System.

"**Capital Lease Obligations**" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are required to be classified and accounted for as a capital lease on the balance sheet of such Person under generally accepted accounting principles and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with generally accepted accounting principles.

"**Code**" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"**Debtor Relief Laws**" means the Bankruptcy Code of the United States, and all other liquidation, conservatorship, bankruptcy, assignment for the benefit of creditors, moratorium, rearrangement, receivership, insolvency, reorganization, or similar debtor relief laws of the United States or other applicable jurisdictions from time to time in effect and affecting the rights of creditors generally.

"**Defaulting Bank**" means any Bank, as reasonably determined by the Administrative Agent or if the Administrative Agent is the Defaulting Bank, by the Required Banks, that (a) has defaulted in its obligation to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement, (b) has notified the Company, the Administrative Agent, the Issuing Bank or any Bank in writing of its intention not to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement, (c) has otherwise failed to pay over to the Administrative Agent or any other Bank any other amount required to be paid by it thereunder within three (3) Business Days of the date when due, (d) has failed, within three (3) Business Days after request by the Administrative Agent, or if the

Administrative Agent is the Defaulting Bank, by the Required Banks, to confirm that it will comply with the terms of the Reimbursement Agreement relating to its obligations to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement or (e) shall (or whose parent company shall) generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or shall have had any proceeding instituted by or against such Bank (or its parent company) seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for, it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 30 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for it or for any substantial part of its property) shall occur, or shall take (or whose parent company shall take) any corporate action to authorize any of the actions set forth above in this clause (e); provided that a Bank shall not be deemed to be a Defaulting Bank solely by virtue of the ownership or assumption of any equity interest in any Bank or any Person that directly or indirectly controls such Bank by a governmental authority or an instrumentality thereof.

"**Equity Participant**" means Security Pacific Capital Leasing Corporation, as Equity Participant, and its successors and assigns.

"**ERISA**" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"**ERISA Affiliate**" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"**Governmental Action**" has the meaning assigned to it in the Facility Lease.

"**Guarantee**" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), *provided* that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "Guarantee" used as a verb has a corresponding meaning.

"**Hedge Agreement**" means any interest rate swap, cap or collar agreement, interest rate future or option contract, currency swap agreement, currency future or option contract, commodity future or option contract, commodity forward contract or other similar agreement.

"**Indebtedness**" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"**Issuing Bank**" means JPMorgan and its successors in their capacity as issuer of the Letter of Credit.

"**JPMorgan**" means JPMorgan Chase Bank, N.A., a national banking association, in its individual capacity, and its successors and assigns.

"**Material Subsidiary**" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of April 16, 2010 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"**Modified Special Casualty Value**" has the meaning assigned to it in the Facility Lease.

"**Multiemployer Plan**" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"**Participant**" has the meaning set forth in Section 15(b) of the Reimbursement Agreement.

"**Participation**" means a participating interest in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a) of the Reimbursement Agreement, but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b) of the Reimbursement Agreement.

"**Participation Amount**" means, with respect to any Bank, the amount set forth in Schedule II to the Reimbursement Agreement opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"**Participation Percentage**" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"**PBGC**" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"**Person**" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"**Plan**" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"**Reimbursement Agreement**" means the Reimbursement Agreement dated as of April 16, 2010 among Arizona Public Service Company, the Banks party thereto, the Administrative Agent and the Issuing Bank, and as the same may be amended and restated from time to time thereafter.

"**Required Banks**" means, at any time, Banks with Participation Percentages aggregating more than 50% at such time exclusive of any Defaulting Bank; provided that if after application of such provision, any Bank shall hold more than 50% of the aggregate Participation Percentages of all Banks at such time (and if there is more than one Bank at such time), "Required Banks" shall mean such Bank plus one additional Bank.

"**Stated Termination Date**" means April 16, 2013 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17 of the Reimbursement Agreement.

"**Subsidiary**" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

"**Termination Date**" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), (v) the date on which the Company delivers a certificate to the Issuing Bank

certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on such date as specified in, and in accordance with the provisions of, the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation.

"**Transaction Documents**" means the Participation Agreement, the Refinancing Agreement, the Indemnity Agreement, the Escrow Deposit Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement and the Notes, each as defined in the Facility Lease.

"**Voting Stock**" means capital stock issued by a corporation, or equivalent interests in any other Person, the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of directors (or persons performing similar functions) of such Person, even if the right so to vote has been suspended by the happening of such a contingency.

SCHEDULE II-A
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

TABLE OF MAXIMUM CREDIT AMOUNTS
SECURITY PACIFIC CAPITAL LEASING CORPORATION

APPLICABLE PERIOD	MAXIMUM CREDIT AMOUNT
From April 16, 2010 through June 30, 2010	$ 27,319,034.00
From July 1, 2010 through January 10, 2011	$ 27,319,034.00
From January 11, 2011 through June 30, 2011	$ 23,205,135.00
From July 1, 2011 through January 10, 2012	$ 23,205,135.00
From January 11, 2012 through June 30, 2012	$ 18,890,092.00
From July 1, 2012 through January 10, 2013	$ 18,890,092.00
From January 11, 2013 through April 16, 2013	$ 14,192,420.00

SCHEDULE II-B
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

TABLE OF MAXIMUM DRAWING AMOUNTS
SECURITY PACIFIC CAPITAL LEASING CORPORATION

APPLICABLE PERIOD	MAXIMUM DRAWING AMOUNT
From April 16, 2010 through June 30, 2010	$ 27,167,373.00
From July 1, 2010 through January 10, 2011	$ 27,319,034.00
From January 11, 2011 through June 30, 2011	$ 23,046,045.00
From July 1, 2011 through January 10, 2012	$ 23,205,135.00
From January 11,2012 through June 30, 2012	$ 18,724,101.00
From July 1, 2012 through January 10, 2013	$ 18,890,092.00
From January 11, 2013 through April 16, 2013	$ 14,192,420.00

SCHEDULE III
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010151

The Issuing Bank shall have the right upon the occurrence of any of the events listed below to terminate the Letter of Credit in accordance with the terms of the Letter of Credit:

(A) The Company shall fail to pay when due any amount payable under Section 2(a) of the Reimbursement Agreement or fail to pay any other amount payable under Section 2 of the Reimbursement Agreement within five (5) Business Days after the same becomes due and payable; or

(B) The Company shall fail to perform or observe (i) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 8(a), 8(b), 8(c) or 8(e) of the Reimbursement Agreement, or (ii) any term, covenant or agreement contained in the Reimbursement Agreement (other than those covered by clause (A) above or subclause (i) of this clause (B) or Section 7(e) or Section 19 of the Reimbursement Agreement) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(C) Any representation or warranty made by the Company in the Reimbursement Agreement or by the Company (or any of its officers) in any certificate delivered in connection with the Reimbursement Agreement shall prove to have been false or misleading in any material respect when made; or

(D) Any material provision of the Reimbursement Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under the Reimbursement Agreement; or

(E) (i) The Company or any of its Material Subsidiaries shall fail to pay (a) any principal of or premium or interest on any Indebtedness that is outstanding in a principal amount of at least $35,000,000 in the aggregate (but excluding Indebtedness owing under the Reimbursement Agreement), or (b) an amount, or post collateral as contractually required in an amount, of at least $35,000,000 in respect of any Hedge Agreement, of the Company or such Material Subsidiary (as the case may be), in each case, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness or Hedge Agreement; or (ii) any event of default shall exist under any agreement or instrument relating to any such Indebtedness and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such event is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(F) The Company or any of its Material Subsidiaries shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least $35,000,000, when the same

becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(G) The Company or any of its Material Subsidiaries shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company or any of its Material Subsidiaries seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any Debtor Relief Law, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company or any of its Material Subsidiaries shall take any corporate action to authorize any of the actions set forth above in this clause (G); or

(H) Judgments or orders for the payment of money that exceeds any applicable insurance coverage (the insurer of which shall be rated at least "A" by A.M. Best Company) by more than $35,000,000 in the aggregate shall be rendered against the Company or any Material Subsidiary and such judgments or orders shall continue unsatisfied or unstayed for a period of 45 days; or

(I) (i) Any "person" or "group" (as such terms are used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended, but excluding any employee benefit plan of such person or its subsidiaries, and any person or entity acting in its capacity as trustee, agent or other fiduciary or administrator of any such plan) becomes the "beneficial owner" (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, as amended), directly or indirectly, of 30% or more of the equity securities of PWCC entitled to vote for members of the board of directors of PWCC; or (ii) during any period of 24 consecutive months, a majority of the members of the board of directors of PWCC cease (other than due to death or disability) to be composed of individuals (a) who were members of that board on the first day of such period, (b) whose election or nomination to that board was approved by individuals referred to in clause (a) above constituting at the time of such election or nomination at least a majority of that board or (c) whose election or nomination to that board was approved by individuals referred to in clauses (a) and (b) above constituting at the time of such election or nomination at least a majority of that board; or (iii) PWCC shall cease for any reason to own, directly or indirectly 80% of the Voting Stock of the Company; or

(J) An event or condition specified in Section 7(g)(iv) of the Reimbursement Agreement shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the

foregoing) which is, in the determination of the Required Banks, likely to exceed $35,000,000 in the aggregate; or

(K) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(L) any event specified in subsection (vii), (viii) or (x) of Section 15 of the Facility Lease shall occur; or

(M) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding $1,000,000 within the periods specified in that Section.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit. This Letter of Credit No. P-010151 (formerly numbered as S-1001) amends and restates our Letter of Credit No. S-1001 dated as of August 15, 1986, as heretofore amended.

EXHIBIT B

FORM OF ASSIGNMENT AND ASSUMPTION AGREEMENT

This Assignment and Assumption Agreement (the "Assignment and Assumption") is dated as of the Effective Date set forth below and is entered into by and between **[***Insert name of Assignor***]** (the "Assignor") and **[***Insert name of Assignee***]** (the "Assignee"). Capitalized terms used herein or in Annex 1 hereto but not defined herein or therein shall have the meanings given to them in the Reimbursement Agreement identified below (as amended, the "Reimbursement Agreement"), receipt of a copy of which is hereby acknowledged by the Assignee. The Terms and Conditions set forth in Annex 1 attached hereto are hereby agreed to and incorporated herein by reference and made a part of this Assignment and Assumption as if set forth herein in full.

For an agreed consideration, the Assignor hereby irrevocably sells and assigns to the Assignee, and the Assignee hereby irrevocably purchases and assumes from the Assignor, subject to and in accordance with the Terms and Conditions and the Reimbursement Agreement, as of the Effective Date inserted by the Administrative Agent as contemplated below, the interest in and to all of the Assignor's rights and obligations in its capacity as a Bank under the Reimbursement Agreement and any other documents or instruments delivered pursuant thereto that represents the amount and percentage interest identified below of all of the Assignor's outstanding rights and obligations under the respective facilities identified below (including without limitation any guaranties included in such facilities and, to the extent permitted to be assigned under applicable law, all claims (including without limitation contract claims, tort claims, malpractice claims, statutory claims and all other claims at law or in equity), suits, causes of action and any other right of the Assignor against any Person whether known or unknown arising under or in connection with the Reimbursement Agreement, any other documents or instruments delivered pursuant thereto or the loan transactions governed thereby) (the "Assigned Interest"). Such sale and assignment is without recourse to the Assignor and, except as expressly provided in this Assignment and Assumption, without representation or warranty by the Assignor.

1. Assignor: _____

2. Assignee: _____

[and is an Affiliate/Approved Fund of **[***identify Bank***]]**[1]

3. Company: Arizona Public Service Company

4. Administrative JPMorgan Chase Bank, N.A., as Administrative

1 Select as applicable.

Agent: Agent under the Reimbursement Agreement

5. Assignee: _____

6. Reimbursement Agreement: The Reimbursement Agreement dated as of April 16, 2010 among Arizona Public Service Company, the Banks party thereto, JPMorgan Chase Bank, N.A., as Issuing Bank and as Administrative Agent.

7. Assigned Interest:

Facility Assigned	Aggregate Amount of Participation Percentages/ Disbursement Advances for all Banks*	Amount of Participation Percentage/ Disbursement Advances Assigned*	Percentage Assigned of Participation Percentage / Aggregate Disbursement Advances[2]
Letter of Credit Facility	$	$	_____%

8. Trade Date: _____[3]

Effective Date: _____, 20_____ **[**TO BE INSERTED BY ADMINISTRATIVE AGENT AND WHICH SHALL BE THE EFFECTIVE DATE OF RECORDATION OF TRANSFER BY THE ADMINISTRATIVE AGENT.**]**

The terms set forth in this Assignment and Assumption are hereby agreed to:

ASSIGNOR

[NAME OF ASSIGNOR**]**

---

* Amount to be adjusted by the counterparties to take into account any payments or prepayments made between the Trade Date and the Effective Date.

2 Set forth, to at least 9 decimals, as a percentage of the Participation Percentages/Disbursement Advances of all Banks thereunder.

3 Insert if satisfaction of minimum amounts is to be determined as of the Trade Date.

By: _____
Title:

ASSIGNEE

[NAME OF ASSIGNEE**]**

By: _____
Title:

[Consented to and**]**[4] Accepted:

JPMORGAN CHASE BANK, N.A., as
Administrative Agent

By: _____
Title:

[Consented to:**]**[5]

ARIZONA PUBLIC SERVICE COMPANY

By: _____
Title:

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4 To be added only if the consent of the Administrative Agent is required by the Reimbursement Agreement.

5 To be added only if the consent of the Company is required by the terms of the Reimbursement Agreement.

ANNEX 1
TERMS AND CONDITIONS FOR
ASSIGNMENT AND ASSUMPTION

1. Representations and Warranties.

1.1 Assignor. The Assignor represents and warrants that (i) it is the legal and beneficial owner of the Assigned Interest, (ii) the Assigned Interest is free and clear of any lien, encumbrance or other adverse claim and (iii) it has full power and authority, and has taken all action necessary, to execute and deliver this Assignment and Assumption and to consummate the transactions contemplated hereby. Neither the Assignor nor any of its officers, directors, employees, agents or attorneys shall be responsible for (i) any statements, warranties or representations made in or in connection with the Reimbursement Agreement, (ii) the execution, legality, validity, enforceability, genuineness, sufficiency, perfection, priority, collectibility, or value of the Reimbursement Agreement, (iii) the financial condition of the Company, any of its Subsidiaries or Affiliates or any other Person obligated in respect of the Reimbursement Agreement, (iv) the performance or observance by the Company, any of its Subsidiaries or Affiliates or any other Person of any of their respective obligations under the Reimbursement Agreement, (v) inspecting any of the property, books or records of the Company, or any guarantor, or (vi) any mistake, error of judgment, or action taken or omitted to be taken in connection with the LC Disbursements or the Reimbursement Agreement.

1.2. Assignee. The Assignee (a) represents and warrants that (i) it has full power and authority, and has taken all action necessary, to execute and deliver this Assignment and Assumption and to consummate the transactions contemplated hereby and to become a Bank under the Reimbursement Agreement, (ii) from and after the Effective Date, it shall be bound by the provisions of the Reimbursement Agreement as a Bank thereunder and, to the extent of the Assigned Interest, shall have the obligations of a Bank thereunder, (iii) agrees that its payment instructions and notice instructions are as set forth in Schedule 1 to this Assignment and Assumption, (iv) confirms that none of the funds, monies, assets or other consideration being used to make the purchase and assumption hereunder are “plan assets” as defined under ERISA and that its rights, benefits and interests in and under the Reimbursement Agreement will not be “plan assets” under ERISA, (v) agrees to indemnify and hold the Assignor harmless against all losses, costs and expenses (including, without limitation, reasonable attorneys’ fees) and liabilities incurred by the Assignor in connection with or arising in any manner from the Assignee’s non-performance of the obligations assumed under this Assignment and Assumption, (vi) it has received a copy of the Reimbursement Agreement, together with copies of financial statements and such other documents and information as it has deemed appropriate to make its own credit analysis and decision to enter into this Assignment and Assumption and to purchase the Assigned Interest on the basis of which it has made such analysis and decision independently and without reliance on the Administrative Agent or any other Bank, and (vii) attached as Schedule 1 to this Assignment and Assumption is any documentation required to be delivered by the Assignee with respect to its tax status pursuant to the terms of the Reimbursement Agreement, duly completed and executed by the Assignee and (b) agrees that (i) it will, independently and without reliance on the Administrative Agent, the Assignor or any other

Bank, and based on such documents and information as it shall deem appropriate at the time, continue to make its own credit decisions in taking or not taking action under the Reimbursement Agreement, and (ii) it will perform in accordance with their terms all of the obligations which by the terms of the Reimbursement Agreement are required to be performed by it as a Bank.

2. Payments. The Assignee shall pay the Assignor, on the Effective Date, the amount agreed to by the Assignor and the Assignee. From and after the Effective Date, the Administrative Agent shall make all payments in respect of the Assigned Interest (including payments of principal, interest, fees and other amounts) to the Assignor for amounts which have accrued to but excluding the Effective Date and to the Assignee for amounts which have accrued from and after the Effective Date.

3. General Provisions. This Assignment and Assumption shall be binding upon, and inure to the benefit of, the parties hereto and their respective successors and assigns. This Assignment and Assumption may be executed in any number of counterparts, which together shall constitute one instrument. Delivery of an executed counterpart of a signature page of this Assignment and Assumption by telecopy shall be effective as delivery of a manually executed counterpart of this Assignment and Assumption. This Assignment and Assumption shall be governed by, and construed in accordance with, the law of the State of New York.

Exhibit 10.3

REIMBURSEMENT AGREEMENT

among

ARIZONA PUBLIC SERVICE COMPANY

THE BANKS PARTY HERETO

and

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent and Issuing Bank

dated as of April 16, 2010

J.P. Morgan Securities Inc. and Union Bank, N.A.,
Joint Lead Arrangers and Joint Bookrunners

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The Table of Contents is not a part of this Agreement.

REIMBURSEMENT AGREEMENT

REIMBURSEMENT AGREEMENT among ARIZONA PUBLIC SERVICE COMPANY, JPMORGAN CHASE BANK, N.A., as Administrative Agent and as Issuing Bank, and the BANKS listed on the signature pages hereto, dated as of April 16, 2010. (Unless otherwise indicated, all capitalized terms used herein have the meanings referred to or set forth in Section 1.)

WHEREAS, the Company has entered into a Participation Agreement dated as of August 1, 1986 (as amended and in effect on April 16, 2010, the "**Participation Agreement**") among the Company, U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston), for itself and as Owner Trustee (together with its successors in such capacity, the "**Owner Trustee**"), The Bank of New York Mellon (as successor to JPMorgan, as successor to Chemical Bank), for itself and as Indenture Trustee (together with its successors in such capacity, the "**Indenture Trustee**"), PVNGS Funding Corp., Inc., PVNGS II Funding Corp., Inc. and Emerson Finance LLC, as Equity Participant (together with its successors and assigns, the "**Equity Participant**"), relating to the acquisition of an undivided interest in PVNGS Unit 2 through a trust for the benefit of the Equity Participant which interest has been leased to the Company pursuant to a lease dated as of August 1, 1986 between the Owner Trustee and the Company (as amended and in effect on April 16, 2010, the "**Facility Lease**");

WHEREAS, pursuant to Section 10(b)(3)(ix) of the Participation Agreement, the Company has agreed to maintain at all times during the Basic Lease Term (as defined in the Participation Agreement) an irrevocable letter of credit for the benefit of the Equity Participant;

WHEREAS, in order to comply with the requirements of Section 10(b)(3)(ix) of the Participation Agreement, the Company entered into a Reimbursement Agreement dated as of August 1, 1986 (as amended and restated thereafter from time to time prior to July 22, 2002, further amended and restated as of July 22, 2002, as further amended and restated as of May 19, 2005, and in effect immediately prior to April 16, 2010, the "**Existing Reimbursement Agreement**") between the Company and JPMorgan, pursuant to which JPMorgan issued to the Equity Participant its irrevocable transferable letter of credit (such letter of credit, as amended and restated and in effect from time to time before May 19, 2005, as further amended and restated as of May 19, 2005, as further amended and restated as of April 16, 2010, and as the same may be amended in accordance with this Agreement and in effect from time to time hereafter, and any successor Letter of Credit as provided in such Letter of Credit, being referred to herein as the "**Letter of Credit**"), to secure the payment of Rent (as defined in the Participation Agreement) by the Company under the Facility Lease to the extent of the amount available to be drawn from time to time under the Letter of Credit;

WHEREAS, the Letter of Credit will expire on May 19, 2010, if not extended; and

WHEREAS, the Company has requested that the Letter of Credit be deemed to be issued pursuant to this Agreement as of the date hereof and immediately amended and restated in substantially the form of Exhibit A hereto to provide, inter alia, that the term of the Letter of

Credit be extended for three years, and the Banks are willing to comply with such requests on the terms and conditions set forth below;

NOW, THEREFORE, in consideration of the premises and in order to induce the Banks to agree to deem the Letter of Credit to be issued pursuant to this Agreement and to amend and restate the Letter of Credit, including to extend the term of the Letter of Credit, the parties hereto agree, upon satisfaction of the conditions set forth in Section 3(b) below and subject to Section 3(c) below, as follows:

Section 1. *Definitions; Accounting Terms*. (a) Definitions. Capitalized terms used herein and not otherwise defined herein have the respective meanings assigned thereto in Appendix A to the Facility Lease. The following terms as used herein have the following respective meanings:

"**ACC**" means the Arizona Corporation Commission or any successor thereto.

"**Administrative Agent**" means JPMorgan, in its capacity as administrative agent for the Banks hereunder, and its successors in such capacity.

"**Administrative Questionnaire**" means, with respect to each Bank, an administrative questionnaire in the form prepared by the Administrative Agent and submitted to the Administrative Agent (with a copy to the Company) duly completed by such Bank.

"**Affiliate**" means, as to any Person, any other Person that, directly or indirectly, controls, is controlled by or is under common control with such Person or is a director or officer of such Person.

"**Agent Parties**" has the meaning given in Section 11(d).

"**Agreement**" means, when used with reference to this Agreement, this Reimbursement Agreement, as the same may be amended in accordance with its terms from time to time.

"**Amended and Restated Letter of Credit**" means the Amended and Restated Irrevocable Transferable Letter of Credit No. P-010152 (formerly numbered as S-1002), dated as of April 16, 2010, amending the Existing Letter of Credit, substantially in the form of Exhibit A hereto.

"**Applicable Booking Office**" means, as to each Bank, its office, branch or affiliate located at its address set forth in its Administrative Questionnaire (or identified in its Administrative Questionnaire as its Applicable Booking Office) or such other office, branch or affiliate of such Bank as it may hereafter designate as its Applicable Booking Office by notice to the Company and the Administrative Agent.

"**Assignee**" has the meaning set forth in Section 15(a).

"**Assignment and Assumption**" means an assignment and assumption entered into by a Bank and an Assignee (with the consent of any party whose consent is required by Section 15), and accepted by the Administrative Agent, substantially in the form of Exhibit B attached hereto.

"**Authorized Officer**" means the chairman of the board, chief executive officer, president, chief financial officer, chief operating officer, chief accounting officer, treasurer, controller, any vice president or any assistant treasurer of the Company.

"**Bank**" means (i) each bank or financial institution listed on the signature pages hereof, each Assignee that becomes a Bank pursuant to Section 15(a), and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"**Base Rate**" means, for any day, a rate per annum equal to the greatest of (a) the Prime Rate in effect on such day, (b) the Federal Funds Rate in effect on such day plus ½ of 1% and (c) the LIBO Rate for a one month interest period on such day (or if such day is not a Business Day, the immediately preceding Business Day) plus 1%. Any change in the Base Rate due to a change in the Prime Rate, the Federal Funds Rate or the LIBO Rate shall be effective from and including the effective date of such change in the Prime Rate, the Federal Funds Rate or the LIBO Rate, respectively.

"**Base Rate Margin**" means a rate per annum determined in accordance with Schedule I hereto.

"**Business Day**" means any day except (i) a Saturday or Sunday, (ii) any other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California or, for purposes of Sections 2(a), 2(g) and 9(i) only, Phoenix, Arizona, are authorized by law to close, or (iii) a day on which payments in respect of the Letter of Credit cannot be funded via wire through the Federal Reserve System.

"**Capital Lease Obligations**" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are required to be classified and accounted for as a capital lease on the balance sheet of such Person under GAAP and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with GAAP.

"**Code**" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"**Company**" means Arizona Public Service Company, an Arizona corporation, and its successors and permitted assigns.

"**Company Materials**" has the meaning given in Section 7(g).

"**Consolidated**" has the meaning set forth in Section 8(e).

"**Consolidated Capitalization**" has the meaning set forth in Section 8(e).

"**Consolidated Indebtedness**" has the meaning set forth in Section 8(e).

"**Consolidated Net Worth**" has the meaning set forth in Section 8(e).

"**Consolidated Subsidiary**" means at any date any Subsidiary or other entity the accounts of which would be consolidated with those of the Company in its consolidated financial statements if such statements were prepared as of such date.

"**Date of Early Termination**" has the meaning set forth in the Letter of Credit.

"**Debtor Relief Laws**" means the Bankruptcy Code of the United States, and all other liquidation, conservatorship, bankruptcy, assignment for the benefit of creditors, moratorium, rearrangement, receivership, insolvency, reorganization, or similar debtor relief laws of the United States or other applicable jurisdictions from time to time in effect and affecting the rights of creditors generally.

"**Defaulting Bank**" means any Bank, as reasonably determined by the Administrative Agent or if the Administrative Agent is the Defaulting Bank, by the Required Banks, that (a) has defaulted in its obligation to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement, (b) has notified the Company, the Administrative Agent, the Issuing Bank or any Bank in writing of its intention not to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement, (c) has otherwise failed to pay over to the Administrative Agent or any other Bank any other amount required to be paid by it hereunder within three (3) Business Days of the date when due, (d) has failed, within three (3) Business Days after request by the Administrative Agent, or if the Administrative Agent is the Defaulting Bank, by the Required Banks, to confirm that it will comply with the terms of this Agreement relating to its obligations to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under this Agreement or (e) shall (or whose parent company shall) generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or shall have had any proceeding instituted by or against such Bank (or its parent company) seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for, it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 30 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for it or for any substantial part of its property) shall occur, or shall take (or whose parent company shall take) any corporate action to authorize any of the actions set forth above in this clause (e); provided that a Bank shall not be deemed to be a Defaulting Bank solely by virtue of the ownership or assumption of any equity interest in any Bank or any Person that directly or indirectly controls such Bank by a governmental authority or an instrumentality thereof.

"**Disbursement Advance**" has the meaning set forth in Section 2(a).

"**Effective Date**" has the meaning set forth in Section 3(b).

"**Eligible Institution**" means (i) a commercial bank or a savings and loan association having a net worth in excess of $250,000,000 (or the equivalent in any other currency), (ii) a Bank or an affiliate of a Bank or (iii) any other Person which the Company designates as an Eligible Institution with the consent of the Administrative Agent.

"**Equity Participant**" has the meaning set forth in the first recital hereto.

"**ERISA**" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"**ERISA Affiliate**" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"**Existing Letter of Credit**" means the Letter of Credit, as amended and in effect immediately prior to April 16, 2010.

"**Existing Reimbursement Agreement**" has the meaning set forth in the third recital hereto.

"**Facility Lease**" has the meaning set forth in the first recital hereto.

"**Federal Funds Rate**" means, for any day, the rate per annum (rounded upward, if necessary, to the nearest 1/100th of 1%) equal to the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day, *provided* that (i) if such day is not a Business Day, the Federal Funds Rate for such day shall be such rate on such transactions on the next preceding Business Day as so published on the next succeeding Business Day, and (ii) if no such rate is so published on such next succeeding Business Day, the Federal Funds Rate for such day shall be the average rate quoted to the Administrative Agent on such day as determined by the Administrative Agent.

"**Fee Letter**" means the Fee Letter dated as of March 17, 2010, among the Company, JPMorgan, J.P. Morgan Securities Inc. and Union Bank, N.A.

"**Financial Information**" means the annual report of the Company on Form 10-K for the year ended December 31, 2009, as filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended, and (ii) the Company's current reports on Form 8-K filed January 25, 2010, February 1, 2010, February 19, 2010, March 3, 2010 and March 4, 2010, as so filed.

"**GAAP**" has the meaning given in Section 1(b).

"**Guarantee**" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), *provided* that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "**Guarantee**" used as a verb has a corresponding meaning.

"**Hedge Agreement**" means any interest rate swap, cap or collar agreement, interest rate future or option contract, currency swap agreement, currency future or option contract, commodity future or option contract, commodity forward contract or other similar agreement.

"**Indebtedness**" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"**Indemnified Party**" has the meaning set forth in Section 21.

"**Indenture Trustee**" has the meaning set forth in the first recital hereto.

"**Instruction**" has the meaning set forth in Section 18(b).

"**ISP**" means International Standby Practices 1998 (International Chamber of Commerce Publication No. 590).

"**Issuing Bank**" means JPMorgan and its successors in their capacity as issuer of the Letter of Credit.

"**JPMorgan**" means JPMorgan Chase Bank, N.A., a national banking association, in its individual capacity, and its successors and assigns.

"**LC Disbursement**" has the meaning given in Section 2(a).

"**Letter of Credit**" has the meaning set forth in the third recital hereto.

"**Letter of Credit Commission Rate**" means a rate per annum determined in accordance with Schedule I hereto.

"**LIBO Rate**" means, as of any date of determination, the rate appearing on Reuters Screen LIBOR01 Page (or on any successor or substitute page of such service, or any successor to or substitute for such service, providing rate quotations comparable to those currently provided on such page of such service, as determined by the Administrative Agent from time to time for purposes of providing quotations of interest rates applicable to deposits in dollars in the London interbank market) at approximately 11:00 a.m., London time, on such date of determination, as the rate for deposits in dollars with a one-month maturity. In the event that such rate is not available at such time for any reason, then the "LIBO Rate" shall be the rate at which deposits in dollars in an amount equal to $5,000,000 and for a one-month maturity are offered by the principal London office of the Administrative Agent in immediately available funds in the London interbank market at approximately 11:00 a.m., London time, on such date of determination.

"**Lien**" means any lien, security interest or other charge or encumbrance of any kind, including, without limitation, the lien or retained security title of a conditional vendor and any easement, right of way or other encumbrance on title to real property.

"**Material Subsidiary**" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of April 16, 2010 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"**Maximum Credit Amount**" means, at any date, the Maximum Credit Amount, as defined in the Letter of Credit.

"**Maximum Drawing Amount**" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"**Multiemployer Plan**" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"**1986 Order**" means Decision No. 55120, dated July 24, 1986, of the ACC.

"**Other Taxes**" has the meaning set forth in Section 2(e).

"**Owner Trustee**" has the meaning set forth in the first recital hereto.

"**Parent**" means, as to any Bank, any Person controlling such Bank.

"**Participant**" has the meaning set forth in Section 15(b).

"**Participation**" means a participating interest of a Bank in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a), but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b).

"**Participation Agreement**" has the meaning set forth in the first recital hereto.

"**Participation Amount**" means, with respect to any Bank, the amount set forth in Schedule II hereto opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"**Participation Percentage**" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"**PBGC**" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"**Permitted Lien**" of the Company or any Material Subsidiary means any of the following:

(i) Liens for taxes, assessments or other governmental charges or levies not at the time delinquent or thereafter payable without penalty or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with GAAP shall have been made;

(ii) Liens imposed by or arising by operation of law, such as Liens of carriers, warehousemen, mechanics, materialmen and landlords incurred in the ordinary course of business, including, without limitation, landlord's liens arising under Arizona law under leases entered into by the Company in the 1986 sale and leaseback transactions with respect to PVNGS Unit 2 and securing the payment of rent under such leases, in each case, for sums not overdue for a period of more than 30 days or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with GAAP shall have been made;

(iii) Liens incurred in the ordinary course of business in connection with worker's compensation, unemployment insurance or other forms of governmental insurance or benefits or other similar statutory obligations;

(iv) Liens to secure obligations on surety or appeal bonds;

(v) Liens on cash deposits in the nature of a right of setoff, banker's lien, counterclaim or netting of cash amounts owed arising in the ordinary course of business on deposit accounts, commodity accounts or securities accounts;

(vi) easements, restrictions, reservations, licenses, covenants, and other defects of title that are not, in the aggregate, materially adverse to the use of such property for the purpose for which it is used;

(vii) Liens securing claims against or other obligations of any Person other than the Company or any Subsidiary of the Company neither assumed nor guaranteed by the Company or any Subsidiary of the Company nor on which the Company or any Subsidiary of the Company customarily pays interest, existing upon real estate or rights

in or relating to real estate acquired by the Company or any Subsidiary of the Company for use in the operation of the business of the Company or any Subsidiary of the Company, including, without limitation, for the generation, transmission or distribution of electric energy, transportation, telephonic, telegraphic, radio, wireless or other electronic communication or any other purpose;

(viii) rights reserved to or vested in and Liens on assets arising out of obligations or duties to any municipality or public authority with respect to any right, power, franchise, grant, license or permit, or by any provision of law;

(ix) rights reserved to or vested in others to take or receive any part of the power pursuant to firm power commitment contracts, purchased power contracts, tolling agreements and similar agreements, coal, gas, oil or other minerals, timber or other products generated, developed, manufactured or produced by, or grown on, or acquired with, any property of the Company;

(x) rights reserved to or vested in any municipality or public authority to control or regulate any property of the Company, or to use such property in a manner that does not materially impair the use of such property for the purposes for which it is held by the Company;

(xi) security interests granted in favor of the lessors in the Company's Decommissioning Trust Agreement (PVNGS Unit 2) dated as of January 31, 1992 (such agreement, as amended or otherwise modified from time to time, being the "Unit 2 Trust Agreement") entered into in connection with the PVNGS Unit 2 sale leaseback transaction to secure the Company's obligations in respect of the decommissioning of PVNGS Unit 2 or related facilities;

(xii) Liens that may exist with respect to the Unit 2 Trust Agreement (other than as described in clause (xi) above) or with respect to either of the Company's Decommissioning Trust Agreement (PVNGS Unit 1) or Decommissioning Trust Agreement (PVNGS Unit 3), each dated as of July 1, 1991, as amended or otherwise modified from time to time, relating to the Company's obligation to set aside funds for the decommissioning and retirement from service of such Units;

(xiii) pledges of pollution control bonds and related rights to secure the Company's reimbursement obligations in respect of letters of credit, bond insurance, and other credit or liquidity enhancements supporting pollution control bond transactions, provided that such pollution control bonds are not secured by any other assets of the Company or any Material Subsidiary;

(xiv) rights and interests of Persons other than the Company or any Material Subsidiary (including, without limitation, acquisition rights), related obligations of the Company or any Material Subsidiary and restrictions on it or its property arising out of contracts, agreements and other instruments to which the Company or any Material Subsidiary is a party that relate to the common ownership or joint use of property or other use of property for the benefit of one or more third parties or that allow a third

party to purchase property of the Company or any Material Subsidiary and all Liens on the interests of Persons other than the Company or any Material Subsidiary in such property;

(xv) transfers of operational or other control of facilities to a regional transmission organization or other similar body and Liens on such facilities to cover expenses, fees and other costs of such an organization or body;

(xvi) Liens established on specified bank accounts of the Company to secure the Company's reimbursement obligations in respect of letters of credit supporting commercial paper issued by the Company and similar arrangements for collateral security with respect to refinancings or replacements of the same;

(xvii) rights of transmission users or any regional transmission organizations or similar entities in transmission facilities;

(xviii) Liens on property of the Company sold in a transaction permitted by Section 8(a) hereof to another Person pursuant to a conditional sales agreement where the Company retains title;

(xix) Liens created under this Agreement;

(xx) Liens on cash or cash equivalents not to exceed $200,000,000 (A) deposited in margin accounts with or on behalf of futures contract brokers or paid over to other contract counterparties, or (B) pledged or deposited as collateral to a contract counterparty to secure obligations with respect to (1) contracts (other than for Indebtedness) for commercial and trading activities in the ordinary course of business for the purchase, transmission, distribution, sale, storage, lease or hedge of any energy or energy related commodity or (2) Hedge Agreements;

(xxi) Liens granted on cash or cash equivalents to defease Indebtedness of the Company or any of its Subsidiaries;

(xxii) Liens granted on cash or cash equivalents constituting proceeds from any sale or disposition of assets that is not prohibited by Section 8(a) deposited in escrow accounts or otherwise withheld or set aside to secure obligations of the Company or any Subsidiary providing for indemnification, adjustment of purchase price or any similar obligations, in each case, in an amount not to exceed the amount of gross proceeds received by the Company or any Subsidiary in connection with such sale or disposition;

(xxiii) Liens, deposits and similar arrangements to secure the performance of bids, tenders or contracts (other than contracts for borrowed money), public or statutory obligations, performance bonds and other obligations of a like nature incurred in the ordinary course of business by the Company or any of its Subsidiaries;

(xxiv) rights of lessees arising under leases entered into by the Company or any of its Subsidiaries as lessor, in the ordinary course of business;

(xxv) any Liens on or reservations with respect to governmental and other licenses, permits, franchises, consents and allowances;

(xxvi) Liens on property which is the subject of a Capital Lease Obligation designating the Company or any of its Subsidiaries as lessee and all right, title and interest of the Company or any of its Subsidiaries in and to such property and in, to and under such lease agreement, whether or not such lease agreement is intended as a security;

(xxvii) licenses of intellectual property entered into in the ordinary course of business;

(xxviii) Liens solely on any cash earnest money deposits made by the Company or any of its Subsidiaries in connection with any letter of intent or purchase agreement permitted hereunder;

(xxix) deposits or funds established for the removal from service of operating facilities and coal mines and related facilities or other similar facilities used in connection therewith; and

(xxx) Liens on cash deposits used to secure letters of credit under defaulting lender provisions in credit or reimbursement facilities;

provided, *however*, that no Lien in favor of the PBGC shall, in any event, be a Permitted Lien.

"**Person**" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"**Plan**" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"**Platform**" has the meaning given in Section 7(g).

"**Prime Rate**" means the rate of interest per annum publicly announced from time to time by JPMorgan as its prime rate in effect at its principal office in New York City; each change in the Prime Rate shall be effective from and including the date such change is publicly announced as being effective; provided, however that in the event that there is a successor to JPMorgan in its capacity as Administrative Agent pursuant to Section 20(a)(v), then the term "Prime Rate" as used in this Agreement shall mean the prime rate, base rate or other analogous rate of the new Administrative Agent.

"**PVNGS**" means the Palo Verde Nuclear Generating Station.

"**PWCC**" means Pinnacle West Capital Corporation, an Arizona corporation and its successors.

"**Reimbursement Default**" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"**Reimbursement Event of Default**" has the meaning set forth in Section 9.

"**Related Parties**" means, with respect to any specified Person, such Person's Affiliates and the respective directors, officers, employees, agents and advisors of such Person and such Person's Affiliates.

"**Reportable Event**" means any of the events set forth in Section 4043 of ERISA, other than events for which the 30 day notice period has been waived under the final regulations issued under Section 4043, as in effect as of the date of this Agreement (the "Section 4043 Regulations"). Any changes made to the Section 4043 Regulations that become effective after the Effective Date shall have no impact on the definition of Reportable Event as used herein unless otherwise amended by the Company and the Banks.

"**Required Banks**" means, at any time, Banks with Participation Percentages aggregating more than 50% at such time exclusive of any Defaulting Bank; provided that if after application of such provision, any Bank shall hold more than 50% of the aggregate Participation Percentages of all Banks at such time (and if there is more than one Bank at such time), "Required Banks" shall mean such Bank plus one additional Bank.

"**Sale Leaseback Obligation Bonds**" means PVNGS II Funding Corp.'s (i) 8.00% Secured Lease Obligation Bonds, Series 1993, due 2015; (ii) any other bonds issued by or on behalf of the Company in connection with a sale/leaseback transaction; and (iii) any refinancing or refunding of the obligations specified in subclauses (i) and (ii) above.

"**Standard Letter of Credit Practice**" means, for the Issuing Bank, any domestic or foreign law or letter of credit practices generally and customarily applicable in the city in which the Issuing Bank issued the Letter of Credit other than any such practices that conflict with the express terms of the Letter of Credit or this Agreement. Such practices shall be (i) of banks that regularly issue letters of credit in the particular city and (ii) required or permitted under the ISP.

"**Stated Termination Date**" means April 16, 2013 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17.

"**Subsequent Order**" means any decision, order or ruling of the ACC issued after April 16, 2010 that amends, supersedes or otherwise modifies the 1986 Order or any successor decision, order or ruling.

"**Subsidiary**" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

"**Taxes**" has the meaning set forth in Section 2(e).

"**Termination Date**" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), (v) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the date specified in, and in accordance with, the provisions of the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation.

"**United States**" means the United States of America, including the States and the District of Columbia, but excluding its territories and possessions.

"**Voting Stock**" means capital stock issued by a corporation, or equivalent interests in any other Person, the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of directors (or persons performing similar functions) of such Person, even if the right so to vote has been suspended by the happening of such a contingency.

"**Wholly-Owned Subsidiary**" of any Person means any corporation of which all shares of the issued and outstanding capital stock (other than any director's qualifying shares) having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

(b) Accounting Terms. Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared, in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Company's independent public accountants) with the most recent audited Consolidated financial statements of the Company delivered to the

Administrative Agent ("**GAAP**"). If at any time any change in GAAP or in the interpretation thereof would affect the computation of any financial ratio or requirement set forth in this Agreement, and either the Company or the Required Banks shall so request, the Administrative Agent, the Banks and the Company shall negotiate in good faith to amend such ratio or requirement to preserve the original intent thereof in light of such change in GAAP or in the interpretation thereof (subject to the approval of the Required Banks); provided that, until so amended, such ratio or requirement shall continue to be computed in accordance with GAAP prior to such change therein.

Section 2. *Reimbursement*. (a) Subject to the following sentence, the Company agrees to reimburse the Issuing Bank by making a payment to the Administrative Agent for the account of the Issuing Bank for the full amount of any drawing that the Issuing Bank shall have paid under the Letter of Credit (each an "**LC Disbursement**") prior to or immediately upon making by the Issuing Bank of each such LC Disbursement on the date of each such LC Disbursement; provided that any moneys received from the Company in connection with any LC Disbursement shall be applied solely for the purpose of reimbursement of the related LC Disbursement. If the Company does not reimburse such LC Disbursement in full on or prior to the date such LC Disbursement is made by the times provided for herein, such LC Disbursement shall constitute an advance (a "**Disbursement Advance**"). The Company promises to pay to the Administrative Agent, for the account of the Issuing Bank and, to the extent a Bank made a payment pursuant to Section 14 hereof to reimburse the Issuing Bank, such Bank, each Disbursement Advance on the earliest of (i) the fifth (5th) Business Day after the Issuing Bank shall have made the applicable LC Disbursement and (ii) the Stated Termination Date. The unpaid amount of any Disbursement Advance shall bear interest, for each day from and including the date the LC Disbursement giving rise to such Disbursement Advance is made to but excluding the date that the Company reimburses such Disbursement Advance in full:

(i) from and including the date such relevant LC Disbursement is made until but excluding the earlier of (x) the date the Administrative Agent, for the benefit of the Issuing Bank and, to the extent a Bank made payment pursuant to Section 14 hereof to reimburse the Issuing Bank, such Bank, shall have received reimbursement from the Company of such Disbursement Advance and all unpaid amounts under this clause (i) and (y) the fifth Business Day after such relevant LC Disbursement is made, payable on demand, at a rate per annum equal to the Base Rate plus the Base Rate Margin, and

(ii) together with interest on any amount not paid by the Company when due under clause (i) above, from and including the fifth Business Day after the relevant LC Disbursement is made until such Disbursement Advance is paid in full, payable on demand, at a rate per annum equal to 2% per annum above the Base Rate plus the Base Rate Margin;

provided that such interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law. Interest accrued pursuant to this paragraph shall be for the account of the Issuing Bank, except that interest accrued on and after the date of payment by any Bank pursuant to Section 14 to reimburse the Issuing Bank shall be for the account of such Bank to the extent of such payment.

(b) The Company agrees to pay to the Administrative Agent for the account of the Banks ratably in proportion to their Participation Percentages a letter of credit commission computed at the Letter of Credit Commission Rate on the Maximum Credit Amount of the Letter of Credit from and including the Effective Date to, but excluding, the Termination Date. Such commission accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Effective Date.

(c) The Company agrees to pay to the Administrative Agent for the account of the Issuing Bank a fronting fee at the rate per annum heretofore mutually agreed by the Company and the Issuing Bank pursuant to the Fee Letter, on the Maximum Credit Amount of the Letter of Credit from and including the Effective Date to, but excluding, the Termination Date. Such fronting fee accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Effective Date. The Company agrees to pay to the Issuing Bank for its account (i) on or before the fifth Business Day after the Issuing Bank shall have paid any drawing under the Letter of Credit, a drawing fee (inclusive of any wire-transfer fees) in an amount equal to $135, (ii) on or before the date of any extension of the Letter of Credit pursuant to Section 17, an amendment fee, if any, in an amount mutually agreed upon between the Issuing Bank and the Company, and (iii) on or before the date of any transfer of the Letter of Credit, a transfer fee, if any, in an amount set forth on Exhibit 3 to the Letter of Credit.

(d) (i) If after April 16, 2010, the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by any Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal Reserve System) against letters of credit issued by or assets held by, deposits with or for the account of, or credit extended by, any Bank or shall impose on any Bank any other condition regarding this Agreement or the Letter of Credit or its Participation therein, and the result of any of the foregoing is to increase the cost to such Bank of the issuance or maintenance of the Letter of Credit or its Participation therein, or to reduce the amount of any sum received or receivable by such Bank under this Agreement with respect thereto, by an amount deemed by such Bank to be material, then within 30 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to the Administrative Agent for the account of such Bank such additional amount or amounts as will compensate such Bank for such increased cost or reduction.

(ii) If any Bank shall have determined that, after April 16, 2010, the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change in any such law, rule or regulation, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or

comparable agency, has or would have the effect of reducing the rate of return on capital of such Bank (or its Parent) as a consequence of such Bank's obligations hereunder to a level below that which such Bank (or its Parent) could have achieved but for such adoption, change, request or directive (taking into consideration its policies with respect to capital adequacy) by an amount deemed by such Bank to be material, then from time to time, within 30 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to such Bank such additional amount or amounts as will compensate such Bank (or its Parent) for such reduction.

(iii) Each Bank will notify the Company and the Administrative Agent of any event of which it has knowledge, occurring after April 16, 2010 which will entitle such Bank to compensation pursuant to clause (i) or (ii) of this Section 2(d) as promptly as practicable, but in any event within 90 days after such Bank obtains knowledge thereof; provided that, if such Bank fails to give such notice within 90 days after it obtains knowledge of such an event, such Bank shall, with respect to compensation payable in respect of any costs resulting from such event, only be entitled to payment for costs incurred on and after the date that such Bank does give such notice. A certificate of any Bank claiming compensation under this Section 2(d) and setting forth the additional amount or amounts to be paid to it hereunder shall be conclusive in the absence of demonstrable error. In determining such amount, such Bank may use any reasonable averaging and attribution methods.

(e) For the purposes of this Section 2(e), the following terms have the following meanings:

"**Taxes**" means any and all present or future taxes, duties, levies, imposts, deductions, charges or withholdings with respect to any payment by the Company pursuant to this Agreement, and all liabilities with respect thereto, excluding (i) in the case of each Bank and the Administrative Agent, taxes imposed on or measured by its net income, and franchise or similar taxes imposed on it, by the United States, or by the jurisdiction (or any political subdivision thereof) under the laws of which such Bank or the Administrative Agent (as the case may be) is organized or does business or in which its principal executive office is located or, in the case of each Bank, in which its Applicable Booking Office is located, (ii) any branch profits taxes imposed by the United States or any similar tax imposed by any other jurisdiction in which the Company is located, (iii) any backup withholding that is required by the Internal Revenue Code to be withheld from amounts payable to a Bank that has failed to comply with Section 2(e)(iii)(2)(A), and (iv) in the case of each Bank, any United States withholding tax imposed with respect to any payment by the Company pursuant to this Agreement, but only up to the rate (if any) at which United States withholding tax would apply to such payments to such Bank at the time such Bank first becomes a party to this Agreement.

"**Other Taxes**" means any present or future stamp or documentary taxes and any other excise or property taxes, or similar charges or levies, which arise from any payment made pursuant to this Agreement or from the execution or delivery of, or otherwise with respect to, this Agreement or the Letter of Credit.

(i) Any and all payments by the Company to or for the account of any Bank or the Administrative Agent hereunder shall be made without deduction for any Taxes or Other Taxes; *provided* that, if the Company shall be required by law to deduct any Taxes or Other Taxes from any such payments, (A) the sum payable shall be increased as necessary so that after making all required deductions for any Taxes or Other Taxes (including deductions applicable to additional sums payable under this Section) such Bank or the Administrative Agent (as the case may be) receives an amount equal to the sum it would have received had no such deductions been made, (B) the Company shall make such deductions, (C) the Company shall pay the full amount deducted to the relevant taxation authority or other authority in accordance with applicable law and (D) the Company shall furnish to the Administrative Agent the original or a certified copy of a receipt evidencing payment thereof.

(ii) The Company agrees to indemnify each Bank and the Administrative Agent for the full amount of Taxes or Other Taxes (including, without limitation, any Taxes or Other Taxes imposed or asserted by any jurisdiction on amounts payable under this Section) paid by such Bank or the Administrative Agent (as the case may be) and any liability (including penalties, interest and expenses) arising therefrom or with respect thereto. This indemnification shall be paid within 30 days after such Bank or the Administrative Agent (as the case may be) makes demand therefor. Such demand shall be made as promptly as practicable, but in any event within 90 days after such Bank obtains actual knowledge of such event; *provided*, *however*, that if any Bank fails to make such demand within 90 days after such Bank obtains knowledge of such event, such Bank shall, with respect to compensation payable in respect of such event, not be entitled to compensation in respect of the costs and losses incurred between the 90th day after such Bank obtains actual knowledge of such event and the date such Bank makes such demand.

(iii)

(1) Each Bank shall deliver to the Company and to the Administrative Agent, at the time or times prescribed by applicable laws or when reasonably requested by the Company or the Administrative Agent, such properly completed and executed documentation prescribed by applicable laws or by the taxing authorities of any jurisdiction and such other reasonably requested information as will permit the Company or the Administrative Agent, as the case may be, to determine (A) whether or not payments made hereunder are subject to Taxes, (B) if applicable, the required rate of withholding or deduction, and (C) such Bank's entitlement to any available exemption from, or reduction of, applicable Taxes in respect of all payments to be made to such Bank by the Company pursuant to this Agreement or otherwise to establish such Bank's status for withholding tax purposes in the applicable jurisdiction.

(2) Without limiting the generality of the foregoing:

(A) any Bank that is a "United States Person" within the meaning of Section 7701(a)(30) of the Internal Revenue Code, and not an exempt recipient described in Section 6049(b)(4) of the Internal Revenue Code, shall

deliver to the Company and the Administrative Agent executed originals of Internal Revenue Service Form W-9 or such other documentation or information prescribed by applicable laws or reasonably requested by the Company or the Administrative Agent as will enable the Company or the Administrative Agent, as the case may be, to determine whether or not such Bank is subject to backup withholding or information reporting requirements; and

(B) each Bank that is organized under the laws of a jurisdiction other than the United States (including each State thereof and the District of Columbia) (a "Foreign Bank") that is entitled under the Internal Revenue Code or any applicable treaty to an exemption from or reduction of withholding tax with respect to payments hereunder shall deliver to the Company and the Administrative Agent (in such number of copies as shall be requested by the recipient) on or prior to the date on which such Foreign Bank becomes a Bank under this Agreement (and from time to time thereafter upon the request of the Company or the Administrative Agent, but only if such Foreign Bank is legally entitled to do so), whichever of the following is applicable

(I) executed originals of Internal Revenue Service Form W-8BEN claiming eligibility for benefits of an income tax treaty to which the United States is a party,

(II) executed originals of Internal Revenue Service Form W-8ECI,

(III) executed originals of Internal Revenue Service Form W-8IMY and all required supporting documentation,

(IV) in the case of a Foreign Bank claiming the benefits of the exemption for portfolio interest under section 881(c) of the Internal Revenue Code, (x) a certificate to the effect that such Foreign Bank is not (A) a "bank" within the meaning of section 881(c)(3)(A) of the Internal Revenue Code, (B) a "10 percent shareholder" of the Company within the meaning of section 881(c)(3)(B) of the Internal Revenue Code, or (C) a "controlled foreign corporation" described in section 881(c)(3)(C) of the Internal Revenue Code and (y) executed originals of Internal Revenue Service Form W-8BEN, or

(V) executed originals of any other form prescribed by applicable laws as a basis for claiming exemption from or a reduction in United States Federal withholding tax together with such supplementary documentation as may be prescribed by applicable laws to permit the Company or the Administrative Agent to determine the withholding or deduction required to be made.

(3) Each Bank shall promptly notify the Company and the Administrative Agent of any change in circumstances which would modify or render invalid any claimed exemption or reduction.

(iv) For any period with respect to which a Bank has failed to provide the Company or the Administrative Agent with the appropriate forms pursuant to Section 2(e)(iii) (unless such failure is due to a change in treaty, law or regulation occurring subsequent to the date on which such form originally was required to be provided, but only to the extent that the Bank has complied with the law as changed by such treaty, law or regulation), such Bank shall not be entitled to indemnification under Section 2(e)(ii) or (iii) with respect to Taxes imposed by the United States; *provided* that if a Bank, which is otherwise exempt from or subject to a reduced rate of withholding tax, becomes subject to Taxes because of its failure to deliver a form required hereunder, the Company shall take such steps as such Bank shall reasonably request to assist such Bank to recover such Taxes.

(v) If the Company is required to pay additional amounts to or for the account of any Bank pursuant to this Section, then such Bank will change the jurisdiction of its Applicable Booking Office if, in the reasonable judgment of such Bank, such change (A) will eliminate or reduce any such additional payment which may thereafter accrue and (B) is not otherwise materially disadvantageous to such Bank.

(f) If (x) the Company is required pursuant to Section 2(d) or 2(e) to make any additional payment to any Bank (any Bank so affected an "Affected Bank") or (y) any Bank becomes a Defaulting Bank, the Company may elect to replace the Participation Percentage and Participation of such Affected Bank or Defaulting Bank, as applicable, provided that no Reimbursement Event of Default shall have occurred and be continuing at the time of such replacement, and provided further that, concurrently with such replacement, (i) another bank or other entity which is reasonably satisfactory to the Company, the Issuing Bank and the Administrative Agent shall agree, as of such date, to purchase for cash (to the extent of the principal amount of such Affected Bank's or Defaulting Bank's, as applicable, Disbursement Advances and accrued interest and fees and other reimbursable amounts then due and payable) and otherwise assume the Participation Percentage and Participation of, and other obligations then due to, such Affected Bank or Defaulting Bank, as applicable, pursuant to an Assignment and Assumption and to become a Bank for all purposes under this Agreement and to assume all obligations of such Affected Bank or Defaulting Bank, as applicable, to be replaced as of such date and to comply with the requirements of Section 15 applicable to assignments, (ii) the Company shall pay to such Affected Bank or Defaulting Bank, as applicable, in same day funds on the day of such replacement all interest, fees and other amounts then accrued but unpaid to such Affected Bank or Defaulting Bank, as applicable, by the Company hereunder to and including the date of replacement, including without limitation payments due to such Affected Bank or Defaulting Bank, as applicable, under Sections 2(d) and 2(e), in each case to the extent not paid by the purchasing Bank, and (iii) concurrently with the effectiveness of such replacement, such Affected Bank or Defaulting Bank, as applicable, shall be released with respect to its Participation Percentage, such Participation Percentage shall be terminated, and Disbursement Advances assigned by such Affected Bank or Defaulting Bank, as applicable, and shall cease to be a Bank hereunder but shall continue to be entitled to the benefits of, and subject to, those provisions of this Agreement which survive payment of all amounts payable pursuant to Section 2 and termination of the Letter of Credit and this Agreement.

(g) The Company shall make each payment hereunder to the Administrative Agent at its Chicago office, not later than 2:00 p.m. (New York City time) on the date when due in lawful money of the United States of America and in Federal or other funds immediately available in Chicago. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding day that is a Business Day. If the date for any payment of principal is extended by operation of law or otherwise, interest thereon shall be payable for such extended time.

(h) Computations of the letter of credit commission, the fronting fee referred to in Section 2(c), and interest based on the Prime Rate shall be made by the Administrative Agent on the basis of a year of 365 or 366 days, as the case may be, for the actual number of days (including the first day but excluding the last day) elapsed. Computations of all other interest hereunder shall be made by the Administrative Agent on the basis of a year of 360 days for the actual number of days (including the first day but excluding the last day) elapsed.

(i) Provided that the Company shall have delivered notice thereof to the Administrative Agent not less than three Business Days prior to any proposed termination, the Company may terminate this Agreement (other than those provisions which expressly survive termination hereof) upon (i) payment in full of all amounts payable under Section 2, together with accrued and unpaid interest thereof, (ii) cancellation and return of the Letter of Credit, and (iii) the payment in full of all reimbursable expenses and other obligations under this Agreement together with accrued and unpaid interest thereon. No such termination will be made unless the Equity Participant will be provided with a substitute letter of credit as and to the extent required by the Participation Agreement at such time or unless the Equity Participant shall otherwise consent.

(j) Notwithstanding any provision of this Agreement to the contrary, if any Bank becomes a Defaulting Bank, then the following provisions shall apply for so long as such Bank is a Defaulting Bank:

(i) the Company shall not be required to pay any letter of credit commission to such Defaulting Bank pursuant to Section 2(b) with respect to such Defaulting Bank's Participation Percentage; provided that, without prejudice to any rights or remedies of the Issuing Bank or any Bank hereunder, the letter of credit commission payable under Section 2(b) with respect to such Defaulting Bank's Participation Percentage shall be payable to the Issuing Bank until such Defaulting Lender shall cease to be a Defaulting Lender hereunder. For the avoidance of doubt, it is being understood that, the interest payable by the Company pursuant to Section 2(a) shall continue to be payable to the applicable Banks, including the Defaulting Bank, to the extent the Defaulting Bank has funded its Participation Percentage and would be entitled to such interest had it not become a Defaulting Bank;

(ii) the Participation Percentage of such Defaulting Bank shall not be included in determining whether the Required Banks have taken or may take any action hereunder (including any consent to any amendment or waiver pursuant to Section 10), other than any waiver, amendment or modification requiring the consent of all Banks or of each affected Bank;

(iii) for the avoidance of doubt, the Company shall retain and reserve its other rights and remedies respecting each Defaulting Bank; and

(iv) in the event that the Administrative Agent, the Company and the Issuing Bank each agrees that a Defaulting Bank has adequately remedied all matters that caused such Bank to be a Defaulting Bank, then this Section 2(i) shall no longer apply in respect of such rehabilitated Defaulting Bank.

Section 3. *Amendment and Restatement of Letter of Credit; Conditions to Effectiveness; Transitional Provisions*. (a) On the terms and conditions herein set forth, the Issuing Bank agrees to execute and deliver to the Equity Participant on the Effective Date, or, if all of the conditions precedent to the effectiveness of this Agreement shall not have been satisfied by 3:00 p.m., New York City time, on the Effective Date, on the next succeeding Business Day, the Amended and Restated Letter of Credit substantially in the form of Exhibit A hereto, amending and restating the Existing Letter of Credit.

(b) This Agreement shall become effective on the date (the "**Effective Date**") on which all of the following conditions shall have been satisfied (or waived in accordance with Section 10):

(i) receipt by the Administrative Agent of a counterpart of this Agreement signed by each party hereto;

(ii) receipt by the Administrative Agent of fees payable by the Company on or before the Effective Date in such amounts and for the accounts of such parties as heretofore mutually agreed pursuant to the Fee Letter;

(iii) receipt by the Administrative Agent of evidence to its satisfaction that all amounts accrued and unpaid under the Existing Reimbursement Agreement to (but not including) the Effective Date payable by any party thereto have been paid and the Existing Reimbursement Agreement shall have been terminated;

(iv) receipt by the Administrative Agent of an opinion of Snell & Wilmer L.L.P., special counsel for the Company, dated the Effective Date, in form and substance satisfactory to the Administrative Agent;

(v) receipt by the Administrative Agent of copies, certified by the Secretary, an Associate Secretary or an Assistant Secretary of the Company, of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance of this Agreement and the transactions contemplated hereby;

(vi) receipt by the Administrative Agent of a certificate of the Secretary, an Associate Secretary or an Assistant Secretary of the Company, dated the Effective Date, certifying the names and true signatures of the officers of the Company authorized to sign this Agreement;

(vii) receipt by the Administrative Agent of a certificate, dated the Effective Date, signed by an Authorized Officer to the effect that (x) (A) no Default or Event of

Default under the Facility Lease, and (B) no Reimbursement Default, in each case, shall have occurred and be continuing on the Effective Date or would result from the amendment and restatement of the Letter of Credit pursuant to clause (a) of this Section 3; and (y) that the representations and warranties of the Company set forth in Section 6 of this Agreement shall be true and correct on and as of the Effective Date as though made on and as of such date;

(viii) receipt by the Administrative Agent of certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency, if any, required for the Company to enter into this Agreement;

(ix) receipt by the Administrative Agent of such other approvals, opinions or documents as the Administrative Agent may reasonably request; and

(x) receipt by the Administrative Agent of all documents the Administrative Agent may reasonably request relating to the existence of the Company, the corporate authority for and the validity of this Agreement and any other matters relevant hereto;

provided that all documents (or copies thereof) to be delivered to the Administrative Agent on or before the Effective Date shall be provided to each Bank and shall be in form and substance satisfactory to the Required Banks.

(c) Promptly after this Agreement becomes effective, the Administrative Agent shall give notice thereof and of the Effective Date to each party hereto. Immediately upon the effectiveness of this Agreement, (1) (A) the Existing Letter of Credit shall be deemed to be issued pursuant to this Agreement, (B) the undrawn amount of the Existing Letter of Credit and any unreimbursed amount of disbursements with respect to the Existing Letter of Credit shall be subject to reimbursement hereunder and (C) the provisions of this Agreement shall apply to the Existing Letter of Credit, and the Company and the Banks hereby expressly acknowledge their respective obligations hereunder with respect to the Existing Letter of Credit, and (2) the Issuing Bank will be obligated to amend and restate the Letter of Credit as provided in clause (a) of this Section 3 and each party hereto will be bound by the provisions of this clause (c).

Section 4. *Adjustment of Maximum Drawing Amount; Terms of Drawing*. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

Section 5. *Obligations Absolute*. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement under all circumstances whatsoever, including, without limitation, the following circumstances:

(i) any lack of validity or enforceability or legal effect of this Agreement, the Letter of Credit or any of the Transaction Documents or Financing Documents;

(ii) any amendment or waiver of or any consent to depart from all or any of this Agreement, the Transaction Documents or Financing Documents;

(iii) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant, the Owner Trustee or any transferee of the Letter of Credit (or any persons or entities for whom any of the foregoing may be acting), the Administrative Agent, any Bank, any Participant or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents, the transactions contemplated hereby or thereby or any unrelated transaction; *provided* that nothing herein shall prevent the assertion of such claim by separate suit or compulsory counterclaim;

(iv) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(v) payment by the Issuing Bank under the Letter of Credit against presentation of a certificate which does not comply with the terms of the Letter of Credit; or

(vi) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

Section 6. *Representations and Warranties of the Company*. The Company represents and warrants as of the Effective Date as follows:

(a) Corporate Existence. Each of the Company and each Material Subsidiary: (i) is a corporation duly organized and validly existing under the laws of the jurisdiction of its incorporation; (ii) has all requisite corporate power necessary to own its assets and carry on its business as presently conducted; (iii) has all governmental licenses, authorizations, consents and approvals necessary to own its assets and carry on its business as presently conducted, if the failure to have any such license, authorization, consent or approval is reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, and except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement and except that (A) the Company from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (B) from time to time communities served by the Company may become incorporated and considerable time may elapse before such a franchise is procured, (C) certain such franchises may have expired prior to the renegotiation thereof, (D) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (E) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope); and (iv) is qualified to do business in all jurisdictions in which the nature of the business conducted by it makes such qualification necessary and where failure so to qualify would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. All of the issued and outstanding common stock of the Company is owned by PWCC.

(b) Noncontravention, Etc. The execution, delivery, and performance by the Company of this Agreement are within the Company's corporate powers, have been duly

authorized by all necessary corporate action, and do not (i) contravene the Company's charter or by-laws, (ii) contravene any Applicable Law or any contractual restriction binding on or affecting the Company, or (iii) cause the creation or imposition of any Lien upon the assets of the Company or any Material Subsidiary.

(c) Approvals. No authorization or approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due execution, delivery and performance by the Company of this Agreement, except for (w) the 1986 Order which has been duly issued by the ACC and is in full force and effect in the form originally issued, (x) such other Governmental Actions as have been duly obtained, given or accomplished, (y) the filing with the ACC of a copy of this Agreement within five business days of the execution hereof, in accordance with the 1986 Order and (z) as may be required under Applicable Law not now in effect. The execution, delivery, and performance by the Company of this Agreement do not require the consent or approval of the Equity Participant or the Owner Trustee (except as specified in this Agreement) or PWCC or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been duly obtained, given or accomplished. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or PVNGS Unit 2 is or will be required in connection with the participation by the Administrative Agent, any Bank or any Participant in the consummation of the transactions contemplated by this Agreement, except such Governmental Actions (A) as have been, duly obtained, given or accomplished or (B) as may be required by Applicable Law not now in effect.

(d) Binding Agreement. This Agreement is a legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(e) Litigation. There is no pending or (to the knowledge of an Authorized Officer of the Company) threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator, that, if adversely determined, would be reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(f) Financial Statements. The balance sheet of the Company and its Consolidated Subsidiaries as of December 31, 2009 and the related statements of income and cash flows of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Banks, fairly present in all material respects the financial condition of the Company and its Consolidated Subsidiaries as of such date and the results of operations and cash flows of the Company and its Consolidated Subsidiaries for such fiscal year, all in accordance with GAAP (except as disclosed therein). Since December 31, 2009, there has been no material

adverse change in the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(g) ERISA. The Company and the ERISA Affiliates have fulfilled their respective obligations under the minimum funding standards of ERISA and the Code with respect to each Plan and are in compliance in all material respects with the presently applicable provisions of ERISA and the Code, and have not incurred any liability to the PBGC or any Plan or Multiemployer Plan, other than liability to the PBGC for premiums prior to the due date for such premiums and liability to any Plan maintained by the Company or an ERISA Affiliate or to any Multiemployer Plan for contributions prior to the due date for such contributions which shall be paid in accordance with the provisions of the minimum funding standards of ERISA and the Code.

(h) Taxes. The Company and its Subsidiaries have filed all United States Federal income tax returns and all other material tax returns which are required to be filed by them and have paid all taxes due pursuant to such returns or pursuant to any assessment received by the Company or any of its Subsidiaries, except to the extent that (i) such taxes are being contested in good faith and by appropriate proceedings and appropriate reserves for the payment thereof have been maintained by the Company and its Subsidiaries in accordance with GAAP or (ii) the failure to make such filings or such payments is not reasonably likely to have a material adverse effect on the financial condition or the financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. The charges, accruals and reserves on the books of the Company and its Material Subsidiaries as set forth in the most recent financial statements of the Company delivered to the Banks pursuant to Section 6(f) in respect of taxes and other governmental charges are, in the opinion of the Company, adequate.

(i) Environmental. The operations and properties of the Company and its Subsidiaries comply in all material respects with all environmental laws, the noncompliance with which would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks prior to the execution and delivery of this Agreement.

(j) Investment Company. The Company is not an “investment company”, or a company “controlled” by an “investment company”, within the meaning of the Investment Company Act of 1940, as amended.

(k) No Material Misstatements or Omissions. The Financial Information did not as of the date furnished, contain any untrue statement of a material fact or omit to state any material fact necessary to make the statements made therein, in the light of the circumstances under which they were or shall be made, not misleading; provided that with respect to any projected financial information, forecasts, estimates or forward-looking information, the Company represents only that such information and materials have been prepared in good faith on the basis of assumptions believed to be reasonable at the time of preparation of such forecasts, and no representation or warranty is made as to the actual attainability of any such projections, forecasts, estimates or forward-looking information.

(l) No Amendments. Except as provided to the Banks prior to the Effective Date, there has been no amendment or waiver of, or consent with respect to, the payment obligations of the Company under any Transaction Document or Financing Document since March 17, 1993.

Section 7. *Affirmative Covenants*. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will, unless the Required Banks shall otherwise consent in writing:

(a) Preservation of Corporate Existence, Business, Etc. (i) Preserve and maintain its corporate existence, rights (charter and statutory) and franchises (other than "franchises" as described in Arizona Revised Statutes, Section 40-283 or any successor provision) reasonably necessary in the normal conduct of its business, if the failure to maintain such rights and privileges is reasonably likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, and use its commercially reasonable efforts to preserve and maintain such franchises reasonably necessary in the normal conduct of its business, except that (A) the Company from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (B) from time to time communities served by the Company may become incorporated and considerable time may elapse before such a franchise is procured, (C) certain such franchises may have expired prior to the renegotiation thereof, (D) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (E) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope; *provided, however*, that the Company may consummate any merger or consolidation permitted under Section 8(b).

(ii) Continue to conduct the same general type of business conducted on April 16, 2010.

(b) Compliance with Laws, Etc. (i) Comply, and cause each Material Subsidiary to comply, in all material respects with all applicable laws, rules, regulations and orders of governmental or regulatory authorities if the failure to comply would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(ii) Comply at all times with the 1986 Order and any Subsequent Order, unless the failure to so comply could not affect the validity or enforceability of the indebtedness of the Company pursuant to this Agreement.

(c) Payment of Taxes and Claims. Pay and discharge, and cause each of its Subsidiaries to pay and discharge, before the same shall become delinquent, all taxes, assessments and governmental charges or levies imposed on it or its property; *provided* that neither the Company nor any of its Subsidiaries shall be required to pay or discharge any such tax, assessment, charge or levy (i) that is being contested in good faith and by proper proceedings and as to which adequate reserves are being maintained in accordance with GAAP or (ii) if the failure to pay such tax, assessment, charge or levy is not reasonably likely to have a material

adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(d) Maintenance of Insurance. Maintain, and cause each Material Subsidiary to maintain, insurance, either with responsible and reputable insurance companies or associations, or through its own program of self-insurance, in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which the Company or such Material Subsidiary operates.

(e) Visitation Rights. Permit, and cause each of its Subsidiaries to permit, at any reasonable time and from time to time, any Bank or any of its agents or representatives to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; *provided* that the Company and its Subsidiaries reserve the right to restrict access to any of its properties in accordance with reasonably adopted procedures relating to safety and security; and provided further that the costs and expenses incurred by any Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions shall be, upon the occurrence and during the continuation of a Reimbursement Default, for the account of the Company and, in all other circumstances, for the account of such Bank.

(f) Keeping of Books; Maintenance of Property. Keep, and cause each Material Subsidiary to keep, (i) proper books of record and account, in which full and correct entries shall be made of all financial transactions and the assets and business of the Company and each such Subsidiary in a manner that permits the preparation of financial statements in accordance with GAAP and (ii) all property useful and necessary in its business in good working order and condition (ordinary wear and tear excepted), it being understood that this covenant relates only to the working order and condition of such properties and shall not be construed as a covenant not to dispose of properties.

(g) Reporting Requirements. Furnish to each of the Banks:

(i) as soon as available and in any event within 60 days after the end of each of the first three fiscal quarters of each fiscal year of the Company, (A) for each such fiscal quarter of the Company, statements of income and cash flows of the Company and its Consolidated Subsidiaries for such fiscal quarter and the related balance sheet of the Company and its Consolidated Subsidiaries as at the end of such fiscal quarter, setting forth in each case in comparative form the corresponding figures for the corresponding fiscal quarter in the preceding fiscal year and (B) for the period commencing at the end of the previous fiscal year and ending with the end of such fiscal quarter, statements of income and cash flows of the Company and its Consolidated Subsidiaries for such period setting forth in each case in comparative form the corresponding figures for the corresponding period in the preceding fiscal year; *provided* that so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(i), its report on Form 10-Q for such fiscal quarter. Each set of financial statements provided under this Section 7(g)(i) shall be accompanied by a

certificate of an Authorized Officer, which certificate shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries in accordance with GAAP, consistently applied (except as disclosed therein), as at the end of, and for, such period (subject to normal year-end audit adjustments);

(ii) as soon as available and in any event within 90 days after the end of each fiscal year of the Company, statements of income, changes in common stock equity and cash flows of the Company and its Consolidated Subsidiaries for such year and the related balance sheets of the Company and its Consolidated Subsidiaries as at the end of such year, setting forth in each case in comparative form the corresponding figures for the preceding fiscal year; *provided* that, so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(ii), its report on Form 10-K for such fiscal year. Each set of financial statements provided pursuant to this Section 7(g)(ii) shall be accompanied by an opinion thereon of independent certified public accountants of recognized national standing, which opinion shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries as at the end of, and for, such fiscal year, in accordance with GAAP consistently applied (except as disclosed therein);

(iii) as soon as possible and in any event within five days after an Authorized Officer knows of the occurrence of any Reimbursement Default continuing on the date of such statement, a statement of an Authorized Officer setting forth details of such Reimbursement Default and the action which the Company has taken and proposes to take with respect thereto;

(iv) as soon as possible, and in any event within ten days after an Authorized Officer knows that any of the events or conditions specified below with respect to any Plan or Multiemployer Plan have occurred or exist, a statement signed by an Authorized Officer setting forth details respecting such event or condition and the action, if any, which the Company or its ERISA Affiliate proposes to take with respect thereto (and a copy of any report or notice required to be filed with or given to the PBGC by the Company or an ERISA Affiliate with respect to such event or condition):

(A) any Reportable Event; *provided* that a failure to meet the minimum funding standard of Section 412 of the Code or Section 302 of ERISA shall be a reportable event regardless of the issuance of any waivers in accordance with Section 412(d) of the Code;

(B) the filing under Section 4041(c) of ERISA of a notice of intent to terminate any Plan in a distress termination or the termination of any Plan in a distress termination;

(C) the institution by the PBGC of proceedings under Section 4042 of ERISA for the termination of, or the appointment of a trustee to administer, any

Plan, or the receipt by the Company or any ERISA Affiliate of a notice from a Multiemployer Plan that such action has been taken by the PBGC with respect to such Multiemployer Plan:

(D) the complete or partial withdrawal by the Company or any ERISA Affiliate under Part 1 of Subtitle E of Title IV of ERISA from a Multiemployer Plan, or the receipt by the Company or any ERISA Affiliate of notice from a Multiemployer Plan that it is in reorganization or insolvency pursuant to Section 4241 or 4245 of ERISA or that it intends to terminate or has terminated under Section 4041A of ERISA; and

(E) the institution of a proceeding by a fiduciary of any Multiemployer Plan against the Company or any ERISA Affiliate to enforce Section 515 of ERISA, which proceeding is not dismissed within 45 days;

(v) promptly after (A) any amendment or modification of the 1986 Order or (B) the promulgation, amendment or modification of any Subsequent Order by the ACC, a copy thereof;

(vi) promptly after the sending or filing thereof, copies of all reports and registration statements (other than exhibits thereto and registration statements on Form S-8 or its equivalent) which the Company or any of its Subsidiaries files with the Securities and Exchange Commission or any national securities exchange;

(vii) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the payment obligations of the Company under any Transaction Document or Financing Document;

(viii) promptly after an Authorized Officer becomes aware of the occurrence thereof, notice of any change by Moody's or S&P of their respective Ratings or of the cessation (or subsequent commencement) by Moody's or S&P of publication of their respective Ratings (as such terms are defined on Schedule I hereto); and

(ix) such other information respecting the condition or operations, financial or otherwise, of the Company or any of its Subsidiaries as the Administrative Agent at the request of any Bank may from time to time reasonably request.

The Company will furnish to the Banks, at the time it furnishes each set of financial statements pursuant to Section 7(g)(i) or 7(g)(ii) above, a certificate of an Authorized Officer (x) to the effect that no Reimbursement Default has occurred and is continuing (or, if any Reimbursement Default has occurred and is continuing, describing the same in reasonable detail and describing the action that the Company has taken and proposes to take with respect thereto) and (y) setting forth in reasonable detail the computations necessary to determine whether the Company is in compliance with Section 8(e) as of the end of the relevant fiscal quarter or fiscal year.

Information required to be delivered pursuant to Sections 7(g)(i), (ii) and (vi) above shall be deemed to have been delivered on the date on which the Company provides notice to the

Administrative Agent that such information has been posted on the Company's parent's website on the Internet at www.pinnaclewest.com, at sec.gov/edaux/searches.htm or at another website identified in such notice and accessible by the Banks without charge; provided that (i) such notice may be included in a certificate delivered pursuant to Section 7(g)(i) or (ii) and (ii) the Company shall deliver paper copies of the information referred to in Section 7(g)(i), (ii), and (vi) to any Bank which requests such delivery. Notwithstanding anything contained herein, in every instance the Company shall be required to provide to the Banks copies (which copies may be in electronic PDF format) of certificates of Authorized Officers required under Section 7(g). Subject to the confidentiality provisions set forth in Section 22, the Company hereby acknowledges that the Administrative Agent may make available to the Banks materials and/or information provided by or on behalf of the Company hereunder (collectively, "**Company Materials**") by posting the Company Materials on IntraLinks or another similar electronic system (the "**Platform**").

(h) Filing with ACC. File a copy of this Agreement, as executed by each of the parties hereto, with the ACC within five business days of the execution hereof.

Section 8. *Negative Covenants*. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will not, without the written consent of the Required Banks:

(a) Sale of Assets. Sell, lease, transfer or otherwise dispose of, or permit any of its Material Subsidiaries to sell, lease, transfer or otherwise dispose of, any assets, or grant any option or other right to purchase, lease or otherwise acquire any assets to any Person other than the Company or any Subsidiary of the Company, except (i) dispositions in the ordinary course of business, including, without limitation, sales or other dispositions of electricity and related and ancillary services, other commodities, emissions credits and similar mechanisms for reducing pollution, and damaged, obsolete, worn out or surplus property no longer required or useful in the business or operations of the Company or any of its Subsidiaries, (ii) sale or other disposition of patents, copyrights, trademarks or other intellectual property that are, in the Company's reasonable judgment, no longer economically practicable to maintain or necessary in the conduct of the business of the Company or its Subsidiaries and any license or sublicense of intellectual property that does not interfere with the business of the Company or any Material Subsidiary, (iii) in a transaction authorized by clause (b) of this Section, (iv) individual dispositions occurring in the ordinary course of business which involve assets with a book value not exceeding $5,000,000, (v) sales of assets during the term of this Agreement having an aggregate book value not to exceed 30% of the total of all assets properly appearing on the most recent balance sheet of the Company provided pursuant to Section 6(f) or 7(g)(ii) hereof and (vi) any Lien permitted under Section 8(c).

(b) Mergers, Etc. Merge or consolidate with or into any Person, or permit any Material Subsidiary to do so, except that:

(i) any Material Subsidiary may merge with any Wholly-Owned Subsidiary of the Company;

(ii) any Material Subsidiary may merge into the Company; and

(iii) the Company may merge with, and any Material Subsidiary may merge with, any other Person;

provided that, in each case, immediately after giving effect to such proposed transaction, no Reimbursement Default would exist; and *provided further* that, in the case of any such merger to which the Company is a party, the Company is the surviving corporation and in the case of any such merger to which any Material Subsidiary and any other Person are the parties, such Material Subsidiary is the surviving corporation.

(c) Negative Pledge. Create or suffer to exist, or permit any of its Material Subsidiaries to create or suffer to exist, any Lien on or with respect to any of its properties, whether now owned or hereafter acquired, or assign, or permit any of its Material Subsidiaries to assign, any right to receive income, other than:

(i) Permitted Liens;

(ii) Liens upon or in, or conditional sales agreements or other title retention agreements with respect to, any real or personal property acquired or held by the Company or any Subsidiary in the ordinary course of business to secure the purchase price of such property, or the construction of or improvements to such property, or to secure Indebtedness incurred solely for the purpose of financing the acquisition, construction or improvement of such property to be subject to such Liens (including any Liens placed on such property within 180 days after the latest of the acquisition, completion of construction or improvement of such property), or Liens existing on such property at the time of its acquisition (other than any such Liens created in contemplation of such acquisition that were not incurred to finance the acquisition of such property) or extensions, renewals, refundings or replacements of any of the foregoing for the same or a lesser amount, provided, however, that no such Lien shall extend to or cover any properties of any character other than the property being acquired, constructed or improved and proceeds, improvements and replacements thereof and no such extension, renewal, refunding or replacement shall extend to or cover any properties not theretofore subject to the Lien being extended, renewed, refunded or replaced;

(iii) assignments of the right to receive income, and Liens on property, of a Person existing at the time such Person is merged into or consolidated with the Company or any Subsidiary of the Company or becomes a Subsidiary of the Company;

(iv) Liens with respect to the leases and related documents entered into by the Company in connection with PVNGS Unit 2 and Liens with respect to the leased interests and related rights if the Company reacquires ownership in any of those interests or acquires any of the equity or owner participants' interests in the trusts that hold title to such leased interests, whether or not it also directly assumes the Sale Leaseback Obligation Bonds, and Liens on the Company's interests in the trusts that hold title to such leased interests and related rights in the event that the Company acquires any of the equity or owner participants' interests in such trusts pursuant to a "special transfer" under

the Company's existing PVNGS Unit 2 sale and leaseback transactions and any Liens resulting or deemed to have resulted if the PVNGS Unit 2 leases are required to be accounted for as capital leases in accordance with GAAP;

(v) other assignments of the right to receive income and Liens securing Indebtedness or claims in an aggregate principal amount not to exceed 20% of the Company's total assets as stated on the most recent balance sheet of the Company provided pursuant to Section 6(f) and 7(g) hereof at any time outstanding; and

(vi) the replacement, extension or renewal of any Lien permitted by clause (iii) or (iv) above upon or in the same property theretofore subject thereto or the replacement, extension or renewal (without increase in the amount or change in any direct or contingent obligor) of the Indebtedness secured thereby.

(d) Assignment of Transaction Documents or Financing Documents. Enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents.

(e) Indebtedness. Permit Consolidated Indebtedness to exceed 65% of Consolidated Capitalization at any time.

"**Consolidated**" refers to the consolidation of accounts in accordance with GAAP.

"**Consolidated Capitalization**" means, at any date, the sum as of such date of Consolidated Indebtedness and Consolidated Net Worth.

"**Consolidated Indebtedness**" means, at any date, the Indebtedness of the Company and its Consolidated Subsidiaries determined on a Consolidated basis as of such date.

"**Consolidated Net Worth**" means, at any date, the sum as of such date of (a) the par value (or value stated on the books of the Company) of all classes of capital stock of the Company and its Subsidiaries, excluding the Company's capital stock owned by the Company and/or its Subsidiaries, plus (or minus in the case of a surplus deficit) (b) the amount of the Consolidated surplus, whether capital or earned, of the Company, determined in accordance with GAAP as of the end of the most recent calendar month (excluding the effect on the Company's accumulated other comprehensive income/loss of the ongoing application of Accounting Standards Codification Topic 815).

Section 9. *Reimbursement Events of Default*. If any of the following events ("**Reimbursement Events of Default**") shall occur and be continuing:

(i) The Company shall fail to pay when due any amount payable under Section 2(a) or fail to pay any other amount payable under Section 2 within five (5) Business Days after the same becomes due and payable; or

(ii) The Company shall fail to perform or observe (A) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 8(a), 8(b), 8(c) or 8(e), or (B) any term, covenant or agreement contained in this Agreement (other than those covered by

clause (i) above or subclause (A) of this clause (ii) or Section 7(e) or Section 19) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(iii) Any representation or warranty made by the Company herein or by the Company (or any of its officers) in any certificate delivered in connection with this Agreement shall prove to have been false or misleading in any material respect when made; or

(iv) Any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) (A) The Company or any of its Material Subsidiaries shall fail to pay (1) any principal of or premium or interest on any Indebtedness that is outstanding in a principal amount of at least $35,000,000 in the aggregate (but excluding Indebtedness outstanding hereunder), or (2) an amount, or post collateral as contractually required in an amount, of at least $35,000,000 in respect of any Hedge Agreement, of the Company or such Material Subsidiary (as the case may be), in each case, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness or Hedge Agreement; or (B) any event of default shall exist under any agreement or instrument relating to any such Indebtedness and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such event is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(vi) The Company or any of its Material Subsidiaries shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least $35,000,000, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(vii) The Company or any of its Material Subsidiaries shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company or any of its Material Subsidiaries seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any Debtor Relief Law, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it

(but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company or any of its Material Subsidiaries shall take any corporate action to authorize any of the actions set forth above in this clause (vii); or

(viii) Judgments or orders for the payment of money that exceeds any applicable insurance coverage (the insurer of which shall be rated at least "A" by A.M. Best Company) by more than $35,000,000 in the aggregate shall be rendered against the Company or any Material Subsidiary and such judgments or orders shall continue unsatisfied or unstayed for a period of 45 days; or

(ix) (A) Any "person" or "group" (as such terms are used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended, but excluding any employee benefit plan of such person or its subsidiaries, and any person or entity acting in its capacity as trustee, agent or other fiduciary or administrator of any such plan) becomes the "beneficial owner" (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, as amended), directly or indirectly, of 30% or more of the equity securities of PWCC entitled to vote for members of the board of directors of PWCC; or (B) during any period of 24 consecutive months, a majority of the members of the board of directors of PWCC cease (other than due to death or disability) to be composed of individuals (1) who were members of that board on the first day of such period, (2) whose election or nomination to that board was approved by individuals referred to in clause (1) above constituting at the time of such election or nomination at least a majority of that board or (3) whose election or nomination to that board was approved by individuals referred to in clauses (1) and (2) above constituting at the time of such election or nomination at least a majority of that board; or (C) PWCC shall cease for any reason to own, directly or indirectly 80% of the Voting Stock of the Company; or

(x) An event or condition specified in Section 7(g)(iv) shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the foregoing) which is, in the determination of the Required Banks, likely to exceed $35,000,000 in the aggregate; or

(xi) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(xii) any event specified in subsection (vii), (viii) or (x) of Section 15 of the Facility Lease shall occur; or

(xiii) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding $1,000,000 within the periods specified in that Section.

then, in every such event the Issuing Bank may, and if instructed to do so by the Required Banks the Issuing Bank shall, by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein. The Administrative Agent shall give notice to the Company under Section 9(ii) promptly upon being requested to do so by the Required Banks and will promptly notify each Bank of any such notice given at the request of the Required Banks.

Section 10. *Amendments and Waivers*. No modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any consent to the assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents shall be effective unless the same shall be in writing and signed by (or with the written consent of) the Company and the Required Banks (and, if the rights or duties of the Issuing Bank or the Administrative Agent are affected thereby, by it); provided that no such modification, amendment, waiver or consent shall, unless signed by (or with the written consent of) each Bank affected thereby, (i) increase the Maximum Credit Amount or Maximum Drawing Amount or subject any Bank to any additional obligation under this Agreement or the Letter of Credit, (ii) reduce the principal of or rate of interest on any reimbursement obligation or reduce the letter of credit commission payable under Section 2(b), (iii) postpone the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission, (iv) extend the Stated Termination Date or the Termination Date or (v) change the definition of Required Banks or the provisions of this Section 10 or any provision of this Agreement that requires action by all the Banks. Any waiver of any provision of this Agreement or the Letter of Credit shall be effective only in the specific instance and for the specific purpose for which given.

Section 11. *Notices*. (a) All notices, requests, demands and other communications provided for hereunder shall, unless otherwise stated herein, be in writing (including facsimile transmission, electronic transmission (subject to Section 11(c) below), or similar transmission) and mailed, sent or delivered:

(i) if to the Company, in the case of deliveries, to its street address at 400 North Fifth Street, Phoenix, Arizona 85004; in the case of mailings, to its mailing address at P.O. Box 53999, Phoenix, Arizona 85072-3999, and in the case of facsimile transmission, to telecopy no. (602) 250-5640, in each case to the attention of the Treasurer; and in the case of electronic mail, to lee.nickloy@pinnaclewest.com;

(ii) if to the Administrative Agent, in the case of deliveries or mailings, to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-0090, Chicago, IL 60603, and in the case of facsimile transmission, to telecopy no. (312) 732-1762, in each case to the attention of Nancy Barwig; and in the case of electronic mail, to nancy.r.barwig@jpmorgan.com; with a copy to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-0874, Chicago, IL 60603, and in the case of facsimile transmission, to telecopy no. (312) 325-3150, in each case to the attention of Lisa Tverdek; and in the case of electronic mail, to lisa.tverdek@jpmorgan.com;

(iii) if to the Issuing Bank, in the case of deliveries or mailings, to its address at JPMorgan Chase Bank, N.A., 300 South Riverside Plaza, Mail Code IL1-0236, Chicago, IL 60606-0236, Attention: Standby Letter of Credit Unit, and in the case of facsimile transmission, to telecopy no. (312) 233-2266 and telephone No.: (800) 634-1969, Option 1, in each case to the attention of Manager — Immediate Action Required; and in the case of electronic mail, to standbylc.chi.mc@jpmchase.com; with a copy to its address at JPMorgan Chase Bank, N.A., 10 S. Dearborn St., Mail Code IL1-1650, Chicago, IL 60603, and in the of case facsimile transmission, to telecopy no. (312) 732-2729 and telephone no. (312) 732-2592, in each case to the attention of Phyllis Huggins; and in the case of electronic mail, to phyllis.huggins@jpmorgan.com;

(iv) if to any other Bank, at such address, electronic mail address, or telecopy number as shall be designated by it in its Administrative Questionnaire;

or, as to each party, to such other person and/or to such other address or number as shall be designated by such party in a written notice to each other party. All such notices, requests, demands and other communications shall be effective when mailed or sent, addressed as aforesaid (subject to Section 11(c) below in the case of electronic communications), except that notices to the Administrative Agent shall not be effective until received by the Administrative Agent and any notice to the Equity Participant pursuant to Section 9 shall not be effective until received by the Equity Participant. Notices of any Reimbursement Default shall be sent by the Company to the Administrative Agent by facsimile transmission.

(b) As promptly as practicable after receipt by the Administrative Agent of any notice or other communication delivered hereunder by the Company, the Administrative Agent shall furnish a copy thereof to each Bank, to the extent such notice or other communication is not otherwise required by the terms thereof to be delivered by the Company to each Bank.

(c) Notices and other communications to the Administrative Agent, the Banks and the Issuing Bank hereunder may be delivered or furnished by electronic communications (including e-mail and internet or intranet websites) pursuant to procedures approved by the Administrative Agent and agreed by the Company; *provided* that the foregoing shall not apply to notices pursuant to Sections 2, 14 or 17 unless otherwise agreed by the Administrative Agent and the applicable Bank or to notices pursuant to the Letter of Credit. The Administrative Agent and the Company may, each in its discretion, agree to accept notices and other communications to it hereunder by electronic communications pursuant to procedures approved by it; *provided* that approval of such procedures may be limited to particular notices or communications. Unless the Administrative Agent and the Company shall otherwise agree, notices and other communications sent to an electronic mail address shall be deemed received upon the sender's receipt of an acknowledgement from the intended recipient (such as by the "return receipt requested" function, as available, return electronic mail or other written acknowledgement); *provided* that (x) if such notice or other communication is not sent during the normal business hours of the recipient, such notice or communication shall be deemed to have been sent at the opening of business on the next business day for the recipient, and (y) notices or communications posted to an Internet website shall be deemed received upon the deemed receipt by the intended recipient at its electronic mail address as described in immediately foregoing clause (x) of notification that such notice or communication is available and identifying the website address therefor.

(d) The Platform is provided "as is" and "as available." The Agent Parties (as defined below) do not warrant the accuracy or completeness of the Company Materials or the adequacy of the Platform, and expressly disclaim any liability for errors in or omissions from the Company Materials. No warranty of any kind, express or implied or statutory, is made by any Agent Party in connection with the Company Materials or the Platform. In no event shall the Administrative Agent, its Affiliates, or any partners, directors, officers, employees, agents and advisors of the Administrative Agent or of its Affiliates (collectively, the "**Agent Parties**") have any liability to the Company, any Bank or any other Person for losses, claims, damages, liabilities or expenses of any kind (whether in tort, contract or otherwise) arising out of the Company's or the Administrative Agent's transmission of Company Materials through the Internet, except to the extent that such losses, claims, damages, liabilities or expenses are determined by a court of competent jurisdiction by a final and nonappealable judgment to have resulted from the gross negligence or willful misconduct of such Agent Party.

Section 12. *No Waiver; Remedies*. No failure on the part of the Administrative Agent or any Bank to exercise, and no delay in exercising, any right, power, or privilege hereunder shall operate as a waiver thereof; nor shall any single or partial exercise of any right hereunder preclude any other or further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

Section 13. *Waiver of Right of Setoff*. The Administrative Agent and each Bank hereby waive any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by it to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "**bankruptcy events**"), against any and all of the obligations of the Company now or hereafter existing in respect of any reimbursement obligation of the Company set forth in Section 2(a), *provided* that any such waiver shall be deemed ineffective as and to the extent that the Administrative Agent and each Bank receive, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience (which counsel shall be mutually satisfactory to the Administrative Agent and the Equity Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Administrative Agent or any Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section 13 shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section 13.

Section 14. *Participations of the Banks*. (a) The Issuing Bank hereby sells to each other Bank, and each Bank hereby severally purchases from the Issuing Bank, as of the Effective Date, a Participation in an amount equal to such Bank's Participation Percentage of the Letter of Credit and in each drawing thereunder, all on the terms and conditions set forth herein. Each Bank

acknowledges and agrees that its obligation to acquire participations pursuant to this paragraph in respect of the Letters of Credit is absolute and unconditional and shall not be affected by any circumstance whatsoever, including any amendment, renewal or extension of the Letter of Credit or the occurrence and continuance of a Reimbursement Event of Default, and that each such payment shall be made without any offset, abatement, withholding or reduction whatsoever.

(b) If at any time on or after the Effective Date the Company shall fail to reimburse any LC Disbursement prior to or immediately upon making thereof by the Issuing Bank, such LC Disbursement shall constitute a Disbursement Advance in accordance with Section 2(a), and the Administrative Agent shall promptly (but in any event no later than 2:30 p.m., New York City time, on the date payment is due from the Banks under this Section 14(b)) advise each Bank thereof and of the amount due from the Company and the amount of such Bank's Participation therein, and each Bank shall pay, no later than 4:00 p.m. (New York City time) on such date such Bank's Participation Percentage of such amount by transferring the same in immediately available funds to the Administrative Agent for the account of the Issuing Bank at the Administrative Agent's address specified in Section 11. With respect to any such LC Disbursement, each Bank agrees that the Issuing Bank shall have no responsibility to the Banks other than obtaining the certificates referred to in the Letter of Credit and notifying each Bank thereof. The Administrative Agent shall promptly credit each Bank's account with such Bank's Participation Percentage of (i) all amounts representing principal of, or interest on, any Disbursement Advances, in each case in respect of which such Bank has funded its Participation Percentage in accordance with the foregoing provisions of this Section 14(b) and (ii) letter of credit commissions payable to each Bank pursuant to Section 2(b) of this Agreement and accruing on and after the Effective Date, but, in the case of both clause (i) and clause (ii), only if, when and to the extent received by the Administrative Agent from the Company. All such payments shall be made if, when and to the extent the Administrative Agent receives payment from the Company in respect of any Disbursement Advance and of the letter of credit commission pursuant to Section 2(b) of this Agreement, and in the same funds in which such amounts are received, by credit to an account at a bank located in the United States of America as each Bank shall designate in writing to the Administrative Agent.

(c) If the Administrative Agent should for any reason make any payment to any Bank in anticipation of the receipt of funds from the Company and such funds are not received by the Administrative Agent from the Company on the date payment is due, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such amounts transferred to such Bank by the Administrative Agent in respect of such Bank's Participation plus interest thereon from the day such amounts were transferred by the Administrative Agent to such Bank to but not including the day such amounts are returned by such Bank at a rate per annum equal to the Federal Funds Rate. If the Administrative Agent is required at any time to return to the Company or to a trustee, receiver, liquidator, custodian or other similar official any portion of the payments made by the Company to the Administrative Agent for the account of any Bank, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such payments transferred to such Bank by the Administrative Agent in respect of such Bank's Participation, but without interest on such payments (unless the Administrative Agent is required to pay interest on such amounts to the Person recovering such payments).

(d) Each Bank agrees that if it should receive any amount due to it under this Agreement in respect of its Participation other than from the Administrative Agent, such Bank will remit all of the same to the Administrative Agent to distribute to the Banks pursuant to this Agreement, and such Bank's Participation shall be adjusted to reflect such remittance. Each Bank further agrees to send the Administrative Agent a copy of any notice sent by such Bank to the Company hereunder.

(e) Each Bank acknowledges and represents that it has made its own independent appraisal of the Company, and the business, affairs and financial condition of the Company, based on such documents and information as such Bank has deemed appropriate, and each Bank will continue to be responsible for making its own independent appraisal of such matters, based on such documents and information as such Bank shall deem appropriate at the time, and has not relied upon and will not hereafter rely upon the Administrative Agent or any other Bank or any information prepared, distributed or otherwise made available by the Administrative Agent for such appraisal or other assessment or review of the Company. Each Bank represents, and in granting a Participation to such Bank it is specifically understood and agreed, that such Bank is acquiring its Participation in the Letter of Credit for its own account in the ordinary course of its commercial banking business and not with a view to, or for sale in connection with, any distribution thereof.

Section 15. *Assignees; Participants*. (a) Each Bank shall have the right, with the prior written consent of the Company (which shall not be unreasonably withheld, and shall not be required if a Reimbursement Event of Default has occurred and is continuing) and the prior written consent of the Administrative Agent and the Issuing Bank, to assign all or a pro rata portion of all of its rights and obligations under its Participation at any time and from time to time to one or more Eligible Institutions (each an "**Assignee**"); *provided* that (i) each such Assignee shall assume such rights and obligations and agree, for the benefit of each other party hereto, to be bound by the provisions of, and perform the obligations of a Bank under, this Agreement, pursuant to an Assignment and Assumption and (ii) the aggregate amount of the Participation or Participations assigned to each such Assignee pursuant to this Section 15(a) shall not be less than $5,000,000. Each Bank shall give prompt notice to the Administrative Agent and the Company of each such assignment made by it. For the avoidance of doubt, no assignment by JPMorgan pursuant to this Section 15 shall affect its rights and obligations in its capacity as Issuing Bank.

(b) (i) Each Bank shall also have the right, without the consent of the Company, to grant participating interests in its Participation at any time and from time to time to one or more other financial institutions or other Persons (other than a natural person or the Company or any of the Company's Affiliates or Subsidiaries) (each a "**Participant**"); *provided* that (A) such Bank's obligations under this Agreement shall remain unchanged, (B) such Bank shall remain solely responsible to the other parties hereto for the performance of such obligations and (C) the Company, the Administrative Agent and the other Banks shall continue to deal solely and directly with such Bank in connection with such Bank's rights and obligations under this Agreement. Each such participation granted by a Bank shall be evidenced by a participation agreement in form acceptable to such Bank. Each such participation agreement shall provide that such Bank shall retain the sole right to exercise its rights under this Agreement and to enforce the obligations owed to it hereunder pursuant to its Participation including, without

limitation, the right to consent to any modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents; *provided* that any such participation agreement may provide that such Bank will not, without the consent of the Participant, consent to any modification, amendment or waiver of this Agreement or the Letter of Credit that (w) increases the Maximum Credit Amount or Maximum Drawing Amount or subjects such Bank to any additional obligation under this Agreement or the Letter of Credit, (x) reduces the principal of or rate of interest on any reimbursement obligation or reduces the letter of credit commission payable under Section 2(b), (y) postpones the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission or (z) extends the Stated Termination Date or the Termination Date, in each case subject to such participation.

(ii) Subject to clause (iii) below, the Company agrees that each Participant shall be entitled to the benefits of Sections 2(d) and 2(e) to the same extent as if it were a Bank and had acquired its interest by assignment pursuant to Section 15(a).

(iii) A Participant shall not be entitled to receive any greater payment under Section 2(d) or 2(e) than the applicable Bank would have been entitled to receive with respect to the participating interest granted to such Participant, unless the granting of such interest to such Participant is made with the Company's prior written consent. A Participant organized under the laws of a jurisdiction outside the United States shall not be entitled to the benefits of Section 2(d) or 2(e) unless the Company is notified of the participating interest granted to such Participant and such Participant agrees, for the benefit of the Company, to comply with Section 2(d) or 2(e) as though it were a Bank.

Section 16. *Continuing Obligation; Binding Effect*. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date and (ii) the date upon which all amounts due and owing to the Administrative Agent or any Bank hereunder shall have been paid in full. The obligation of the Company to reimburse the Administrative Agent, the Issuing Bank and the Banks pursuant to Sections 2(d), 2(e), 19 and 21 hereof and the obligations of the parties pursuant to Sections 22, 24 and 27 hereof shall survive the termination of the Letter of Credit and this Agreement. This Agreement shall be binding upon and inure to the benefit of each of the parties hereto and their respective successors. The Company shall not have the right to assign its rights hereunder or any interest herein to any Person without the prior written consent of the Issuing Bank and each Bank. The Issuing Bank shall not have the right to assign its rights as the Issuing Bank hereunder without the prior written consent of the Company (which shall not be unreasonably withheld) and each Bank.

Section 17. *Extension of the Letter of Credit*. At least 105 days but not more than 180 days before the Stated Termination Date, the Company may request the Administrative Agent in writing (each such request being irrevocable and binding), with a copy to the Issuing Bank and each Bank, to extend for not less than three years, nor more than eight years (or, if earlier, the end of the Basic Lease Term or as otherwise required under the Participation Agreement), the Stated Termination Date, specifying the terms and conditions, including fees, to be applicable to such extension. Within 45 days after receiving such extension request (or such later date as the Company may authorize in writing, but in no event later than 60 days before the Stated

Termination Date), each Bank shall notify the Administrative Agent and the Company of its consent or nonconsent to such extension request, and if any Bank shall give no such notice, it shall be deemed not to have consented to such extension request. No such requested extension shall be effective without the consent of all the Banks. The consent of any Bank shall be in its sole discretion and shall be conditional upon no Reimbursement Default or Reimbursement Event of Default existing as of the date of such extension and the preparation, execution and delivery of legal documentation in form and substance satisfactory to such Bank and its counsel, incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement among the Company, and the Banks, and evidence satisfactory to it of the due authorization and validity thereof.

Section 18. *Limited Liability of the Banks*.

(a) The Company assumes all risks of the acts or omissions of the Equity Participant and any beneficiary or transferee of the Letter of Credit with respect to its use of the Letter of Credit. None of the Administrative Agent, the Issuing Bank and the Banks, nor their respective Affiliates nor any officer, director, employee or agent of any of the foregoing shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or any acts or omissions of the Equity Participant or any beneficiary or transferee in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement thereon, even if such documents shall prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Issuing Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except that the Company shall have a claim against the Issuing Bank, and the Issuing Bank shall be liable to the Company, to the extent, but only to the extent, of any direct, as opposed to special, indirect, consequential or punitive, damages or losses suffered by the Company which the Company proves were caused by the Issuing Bank's gross negligence or willful misconduct in (i) honoring a presentation that does not strictly comply with the Letter of Credit, (ii) failing to honor a presentation that strictly complies with the Letter of Credit or (iii) retaining any document presented for purposes of drawing under the Letter of Credit. In no event shall the Issuing Bank be deemed to have failed to act with due diligence or reasonable care if the Issuing Bank's conduct is in accordance with Standard Letter of Credit Practice and in accordance with this Agreement. In furtherance and not in limitation of the foregoing, the Issuing Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Issuing Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

(b) Without limiting any other provision of this Agreement, the Issuing Bank and each other Indemnified Party (if applicable), shall not be responsible to the Company for, and the Issuing Bank's rights and remedies against the Company and the Company's obligation to reimburse the Issuing Bank shall not be impaired by: (i) honor of a presentation under the Letter of Credit which on its face strictly complies with the terms of the Letter of Credit; (ii) honor of a presentation of any documents presented for purposes of drawing under the Letter of Credit (a "**Drawing Document**") which appear on their face to have been signed, presented or issued (X)

by any purported successor or transferee of any beneficiary or other party required to sign, present or issue the Drawing Documents or (Y) under a new name of the beneficiary; (iii) acting upon any communication or instruction (whether oral, telephonic, written, telegraphic, facsimile or electronic) (each an "**Instruction**") that is unauthorized and that is (x) received pursuant to the express terms of the Letter of Credit or (y) any other Instruction regarding the Letter of Credit or error in computer transmission that in either case the Indemnified Party, in Good Faith, believes to have been given by a Person or entity authorized to give such Instruction; (iv) any errors, omissions, interruptions or delays in transmission or delivery of any message, advice or document (regardless of how sent or transmitted) or for reasonable errors in interpretation of technical terms made in good faith after advice of counsel or in translation; (v) any delay in giving or failing to give any notice; (vi) any acts, omissions or fraud by, or the solvency of, any beneficiary, any nominated Person or any other Person other than the Issuing Bank or an Indemnified Party; (vii) any breach of contract between the beneficiary and the Company or any of the parties to the underlying transaction; (viii) assertion or waiver of any provision of the ISP which primarily benefits an issuer of a letter of credit, including, any requirement that any Drawing Document be presented to it at a particular hour or place, except to the extent such provisions of the ISP conflict with the express provisions of the Letter of Credit or this Agreement; (ix) dishonor of any presentation for which the Company is unable or unwilling to reimburse or indemnify the Issuing Bank (provided that the Company acknowledges that if the Issuing Bank shall later be required to honor the presentation, the Company shall be liable therefor in accordance with Article 2 hereof); and (x) acting or failing to act as required or permitted under Standard Letter of Credit Practice. For purposes of this Section 18(b), "**Good Faith**" means honesty in fact in the conduct of the transaction concerned. For the avoidance of doubt, it is understood that this Section 18(b) shall not be construed to limit the Issuing Bank's liability for damages caused by the Issuing Bank's gross negligence or willful misconduct as otherwise provided for in this Agreement.

(c) The Company shall notify the Administrative Agent and the Issuing Bank of (i) any noncompliance with any Instruction given by the Company with respect to the Letter of Credit or any amendment thereto, any other irregularity with respect to the text of the Letter of Credit or any amendment thereto or any claim of an unauthorized, fraudulent or otherwise improper Instruction given by the Company with respect to the Letter of Credit or any amendment thereto, in each case within ten (10) Business Days after an Authorized Officer of the Company becomes aware of the receipt by the Company of a copy of the Letter of Credit or any such amendment and (ii) any objection the Company may have to the Issuing Bank's honor or dishonor of any presentation under the Letter of Credit or any other action or inaction taken or proposed to be taken by the Issuing Bank under or in connection with this Agreement or the Letter of Credit, within ten (10) Business Days after an Authorized Officer of the Company becomes aware of the objectionable action or inaction. To the extent allowed by applicable law, the failure to so notify the Issuing Bank within said times shall discharge the Issuing Bank from any loss or liability that the Issuing Bank could have avoided or mitigated had it received such notice, to the extent that the Issuing Bank could be held liable for damages hereunder; provided that the foregoing shall not be construed to excuse the Issuing Bank from liability to the Company to the extent of any direct damages (as opposed to consequential damages, claims in respect of which are hereby waived by the Company to the extent permitted by applicable law) suffered by the Company that are caused by the Issuing Bank's failure to exercise care when determining whether drafts and other documents presented under the Letter of Credit comply

with the terms thereof or by the Issuing Bank's gross negligence or willful misconduct; provided, further, that, if the Company shall not provide such notice to the Issuing Bank within twenty (20) Business Days of the date of receipt, the Issuing Bank shall have no liability whatsoever for such noncompliance, irregularity, action or inaction and the Company shall be precluded from raising such noncompliance, irregularity or objection as a defense or claim against Issuing Bank. For the avoidance of doubt, it is understood that this Section 18(c) shall not be construed to limit the Issuing Bank's liability for damages caused by the Issuing Bank's gross negligence or willful misconduct as otherwise provided for in this Agreement.

Section 19. *Cost, Expenses and Taxes*. The Company agrees to pay not later than 30 days after demand therefor (a) all reasonable costs and expenses of the Administrative Agent in connection with the preparation, execution, delivery, filing, recording and administration of this Agreement and any other documents which may be delivered in connection with this Agreement and any waiver or consent under, or amendment of, this Agreement, the Fee Letter or any of the Transaction Documents or Financing Documents, including, without limitation, the reasonable fees and out-of-pocket expenses of one firm of attorneys for the Administrative Agent (and any additional firms required to address matters in respect of which such firm is precluded from representation as a result of conflicts) and local counsel who may be retained by said counsel, with respect thereto and with respect to advising the Administrative Agent as to its rights and responsibilities under this Agreement; (b) as to the Administrative Agent, the Issuing Bank and each Bank, all reasonable costs and expenses (including reasonable counsel fees and expenses) in connection with (i) the enforcement of this Agreement and such other documents which may be delivered in connection with this Agreement or (ii) any action or proceeding relating to a court order, injunction or other process or decree restraining or seeking to restrain the Issuing Bank from paying any amount under the Letter of Credit; and (c) as to the Administrative Agent and the Issuing Bank, all reasonable costs and expenses (including reasonable counsel fees and expenses) in connection with each transfer of the Letter of Credit in accordance with its terms. In addition, the Company shall pay any and all stamp, documentary, filing, recording or other similar taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents, and agrees to save the Administrative Agent and each Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, *provided* that the Administrative Agent and each Bank agree promptly to notify the Company of any such taxes and fees which are incurred by the Administrative Agent or such Bank. To the extent permitted by applicable law, the foregoing provisions shall supersede any costs and expenses provisions set forth in Section 8.02 of the ISP.

Section 20. *Administrative Agent; Issuing Bank*. (a)

(i) Each Bank irrevocably appoints and authorizes the Administrative Agent to take such action as agent on its behalf and to exercise such powers under this Agreement as are delegated to the Administrative Agent by the terms hereof, together with all such powers as are reasonably incidental thereto.

(ii) The Administrative Agent shall not have any duties or obligations except those expressly set forth herein. Without limiting the generality of the foregoing, (a) the Administrative Agent shall not be subject to any fiduciary or other implied duties, regardless of

whether a Reimbursement Event of Default has occurred and is continuing, (b) the Administrative Agent shall not have any duty to take any discretionary action or exercise any discretionary powers, except discretionary rights and powers expressly contemplated herein that the Administrative Agent is required to exercise in writing as directed by the Required Banks (or such other number or percentage of the Banks as shall be necessary under the circumstances as provided in Section 10), and (c) except as expressly set forth herein, the Administrative Agent shall not have any duty to disclose, and shall not be liable for the failure to disclose, any information relating to the Company or any of its Subsidiaries that is communicated to or obtained by the bank serving as Administrative Agent or any of its Affiliates in any capacity. The Administrative Agent shall not be liable for any action taken or not taken by it with the consent or at the request of the Required Banks (or such other number or percentage of the Banks as shall be necessary under the circumstances as provided in Section 10), or in the absence of its own gross negligence or willful misconduct. The Administrative Agent shall be deemed not to have knowledge of any Reimbursement Event of Default unless and until written notice thereof is given to the Administrative Agent by the Company or a Bank, and the Administrative Agent shall not be responsible for or have any duty to ascertain or inquire into (i) any statement, warranty or representation made in or in connection with this Agreement, (ii) the contents of any certificate, report or other document delivered hereunder or in connection with this Agreement, (iii) the performance or observance of any of the covenants, agreements or other terms or conditions set forth in this Agreement, (iv) the validity, enforceability, effectiveness or genuineness of this Agreement or any other agreement, instrument or document, or (v) the satisfaction of any condition set forth in Section 3 or elsewhere in this Agreement, other than to confirm receipt of items expressly required to be delivered to the Administrative Agent.

(iii) The Administrative Agent shall be entitled to rely upon, and shall not incur any liability for relying upon, any notice, request, certificate, consent, statement, instrument, document or other writing reasonably believed by it to be genuine and correct and to have been signed or sent by the proper Person. The Administrative Agent also may rely upon any statement made to it orally or by telephone (except when a writing is expressly required) and reasonably believed by it to be made by the proper Person, and shall not incur any liability for relying thereon.

(iv) The Administrative Agent may perform any and all its duties and exercise its rights and powers hereunder by or through any one or more sub-agents appointed by the Administrative Agent in the exercise of reasonable care.

(v) Subject to the appointment and acceptance of a successor Administrative Agent as provided in this paragraph, the Administrative Agent may resign at any time by notifying the Banks and the Company. Upon any such resignation, the Required Banks shall have the right, with the prior written approval of the Company (which approval will not be unreasonably withheld or delayed and which shall be required only so long as no Reimbursement Event of Default shall be continuing), to appoint a successor. If no successor shall have been so appointed by the Required Banks and shall have accepted such appointment within 30 days after the retiring Administrative Agent gives notice of its resignation, then the retiring Administrative Agent may, on behalf of the Banks, appoint a successor Administrative Agent which shall be a commercial bank having capital and retained earnings of at least $100,000,000 or an Affiliate of any such commercial bank. Upon the acceptance of its appointment as Administrative Agent

hereunder by a successor, such successor shall succeed to and become vested with all the rights, powers, privileges and duties of the retiring Administrative Agent, and the retiring Administrative Agent shall be discharged from its duties and obligations hereunder. The fees payable by the Company to a successor Administrative Agent shall be the same as those payable to its predecessor unless otherwise agreed between the Company and such successor. After the Administrative Agent's resignation hereunder, the provisions of this Section 20 and Sections 19 and 21 shall continue in effect for the benefit of such retiring Administrative Agent, its sub agents and their respective Affiliates in respect of any actions taken or omitted to be taken by any of them while it was acting as Administrative Agent.

(vi) Each Bank acknowledges that it has, independently and without reliance upon the Administrative Agent or any other Bank and based on such documents and information as it has deemed appropriate, made its own credit analysis and decision to enter into this Agreement. Each Bank also acknowledges that it will, independently and without reliance upon the Administrative Agent or any other Bank and based on such documents and information as it shall from time to time deem appropriate, continue to make its own decisions in taking or not taking action under or based upon this Agreement or related agreement or any document furnished hereunder.

(b) The Administrative Agent and its Affiliates may accept deposits from, make loans or otherwise extend credit to, and generally engage in any kind of business with, the Company, the Equity Participant and their respective Subsidiaries and Affiliates and receive payment on such loans or extensions of credit and otherwise act with respect thereto freely and without accountability in the same manner as if this Agreement and the transactions contemplated hereby were not in effect.

(c) The Administrative Agent may consult with legal counsel (who may be counsel for the Company), independent public accountants and other experts as it may select and shall not be liable for any action taken or omitted to be taken by it in good faith in accordance with the advice of such counsel, accountants or experts.

(d) It is understood that the Issuing Bank will exercise and give the same care and attention to the Letter of Credit as it gives to its other letters of credit and loans for its own account and that the Issuing Bank shall have no obligation to the Company or any other Bank and no duty or responsibility with respect to this Agreement or the Letter of Credit, except as expressly provided herein and in the Letter of Credit. Without limiting the generality of the foregoing, the Issuing Bank shall not be required to take any action with respect to any Reimbursement Default, except as expressly provided in Section 9 hereof. The Issuing Bank shall not be liable for any action taken or not taken at the request or with the approval of the Required Banks (or all the Banks, as applicable) or for the performance or non-performance of the obligations of any other party under this Agreement or any Transaction Document or Financing Document or any other document contemplated thereby. It is further understood that: (i) except as expressly limited by the provisions of this Agreement, the Issuing Bank retains the sole right to exercise its rights and enforce the obligations of the Company under this Agreement, and the Issuing Bank may use its sole discretion with respect to exercising or refraining from exercising any rights or taking or refraining from taking any actions which may be vested in it or which it may be entitled to take or assert under this Agreement or any of the Transaction

Documents or Financing Documents (including, without limitation, the giving of any notice to any Person of any Reimbursement Event of Default under this Agreement except as provided in Section 9); and (ii) the Issuing Bank shall not, in the absence of gross negligence or willful misconduct, be under any liability to any other Bank with respect to anything which the Issuing Bank may do or refrain from doing in the exercise of its best judgment or which it may deem to be necessary or desirable. Neither the Administrative Agent nor the Issuing Bank shall incur any liability by acting in reliance upon any written communication or any telephone conversation which it reasonably believes to be genuine and correct or to have been signed, sent or made by the proper Person. Neither the Administrative Agent nor the Issuing Bank shall have any obligation to make any claim on, or assert any lien upon, or assert any setoff against, any property held by it and, if it elects to do so, it may in its discretion apply the same against indebtedness of the Company other than the Company's obligations under this Agreement; *provided* that, to the extent any funds received pursuant to any of the foregoing are applied to the obligations of the Company under Section 2(a) or 2(b) hereof, each Bank shall be entitled to receive its pro rata share thereof in accordance with Section 14(b) above. Any such setoff or other action in respect of any reimbursement obligation of the Company set forth in Section 2(a) will be subject to Section 13.

Section 21. *Indemnification*. (a) To the fullest extent permitted by law, the Company shall indemnify and hold harmless the Administrative Agent, the Issuing Bank, each Bank, their respective affiliates and correspondents and each of their respective directors, officers, employees and agents (each such party, an "**Indemnified Party**") from and against any and all claims, suits, judgments, costs, losses, fines, penalties, damages, liabilities, and expenses, including expert witness fees and reasonable legal fees, charges and disbursements of any counsel (including in-house counsel fees and allocated costs) for any Indemnified Party ("**Costs**") (except to the extent any such Costs are expressly stated in this Agreement to be payable by the Indemnified Party or to the extent expressly limited pursuant to Sections 2(d), 2(e), 2(f), 7(e), 18(a) and 19), arising out of, in connection with, or as a result of: (i) the Letter of Credit or any pre-advice of its issuance; (ii) any action or proceeding arising out of or in connection with the Letter of Credit or this Agreement (whether administrative, judicial or in connection with arbitration), including any action or proceeding to compel or restrain any presentation or payment under the Letter of Credit, or for the wrongful dishonor of or honoring a presentation under the Letter of Credit; (iii) any Instruction that is unauthorized and that is (x) received pursuant to the express terms of the Letter of Credit or (y) any other Instruction regarding the Letter of Credit or error in computer transmission that in either case the Indemnified Party reasonably believed to be authorized; (iv) any third party seeking to enforce the rights of an applicant, beneficiary, nominated person, transferee or assignee of proceeds of the Letter of Credit; (v) the fraud, forgery or illegal action of parties other than the Indemnified Party (including, for the avoidance of doubt, any fraud, forgery or illegal action by any party in connection with any transfer of the Letter of Credit); (vi) the enforcement against the Company of this Agreement or any rights or remedies under or in connection with this Agreement or the Letter of Credit; (vii) the Administrative Agent's or the Issuing Bank honoring any presentation upon or during the continuance of any Reimbursement Event of Default or for which the Company is unable or unwilling to make any payment to the Administrative Agent, the Issuing Bank or any Bank as required under this Agreement; (viii) the acts or omissions, whether rightful or wrongful, of any present or future de jure or de facto governmental or regulatory authority or cause or event beyond the control of such Indemnified Party; in each case, including that

resulting from the Administrative Agent's or the Issuing Bank's own negligence, provided, however, that such indemnity shall not be available to any Person claiming indemnification under (i) through (viii) above to the extent that such Costs are found in a final, non-appealable judgment by a court of competent jurisdiction to have resulted directly from the gross negligence or willful misconduct of the Indemnified Party claiming indemnity, in which case any fees or expenses previously paid or advanced by the Company to such Indemnified Party in respect of such indemnified obligation (if any) will be returned by such Indemnified Party. Without limitation of the foregoing, the Company shall not be required to indemnify the Issuing Bank or its Related Parties pursuant to this Section for any Costs to the extent solely caused by (i) the Issuing Bank's willful misconduct or gross negligence in determining whether documents presented under the Letter of Credit comply with the terms of the Letter of Credit or (ii) its willful failure to make lawful payment under the Letter of Credit after presentation to it by the beneficiary of the Letter of Credit of documents strictly complying with the terms and conditions of the Letter of Credit. If and to the extent that the obligations of Company under this paragraph are unenforceable for any reason, Company shall make the maximum contribution to the Costs permissible under applicable law.

(b) To the extent permitted by applicable law, the foregoing provisions shall supersede any indemnity provisions set forth in Section 8.01(b) of the ISP.

(c) To the extent that the Administrative Agent or the Issuing Bank is not reimbursed and indemnified by the Company under this Agreement, each Bank will reimburse and indemnify the Administrative Agent and the Issuing Bank on demand for and against such Bank's Participation Percentage of any and all claims, demands, liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements (including fees and disbursements of counsel) of any kind or nature whatsoever which may be imposed on, incurred by, or asserted against the Administrative Agent or the Issuing Bank in any way relating to or arising out of this Agreement, the Fee Letter, the Letter of Credit, or any of the Transaction Documents or Financing Documents or any action taken or omitted to be taken by the Administrative Agent or the Issuing Bank hereunder or thereunder, or the transactions contemplated hereby and thereby or the enforcement of any of the terms hereof and thereof; *provided* that such Bank shall not be liable for any portion of such claims, demands, liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, out-of-pocket expenses or disbursements resulting from the gross negligence or willful misconduct of the Administrative Agent or the Issuing Bank or which are expressly excluded from the indemnification by the Company by the proviso to the first sentence of Section 21(a), or by the second sentence of Section 21(a) of this Agreement. Each Bank's obligations under this Section 21(c) shall survive the termination of this Agreement and the Letter of Credit. If the Administrative Agent or the Issuing Bank is reimbursed by the Company for any amounts previously received from any Bank pursuant to this Section 21(c), it will promptly pay to such Bank its proportionate share of any amounts so received.

Section 22. *Confidentiality*. (a) The Administrative Agent and each Bank agree (on behalf of themselves and each of their Affiliates, directors, officers, employees and representatives) to take normal and reasonable precautions and exercise due care to maintain the confidentiality of all non-public information provided to them by the Company or any Subsidiary of the Company in connection with this Agreement and neither the Administrative Agent, any

Bank nor any of their Affiliates, directors, officers, employees and representatives shall use any such information for any purpose or in any manner other than pursuant to the terms contemplated by this Agreement, except to the extent such information (a) was or becomes generally available to the public other than as a result of a disclosure by the Administrative Agent or any Bank, or (b) was or becomes available on a non-confidential basis from a source other than the Company, provided that such source is not bound by a confidentiality agreement with the Company known to the Administrative Agent or affected Bank after reasonable inquiry; provided that nothing herein shall limit the disclosure of any such information (i) to the extent required by statute, rule, regulation or judicial process; (ii) to counsel for the Administrative Agent or any Bank; (iii) to bank examiners, auditors or accountants, on a confidential basis; (iv) to the Administrative Agent or any other Bank; (v) by the Administrative Agent or any Bank to an Affiliate thereof who is bound by this Section 22; provided that any such information delivered to an Affiliate shall be for the purposes related to the extension of credit represented by this Agreement and the administration and enforcement thereof and for no other purpose; (vi) in connection with any litigation relating to enforcement of this Agreement or (vii) to any assignee or participant (or prospective assignee or participant) so long as such assignee or participant (or prospective assignee or participant) first enters into a confidentiality agreement with the respective Bank, which confidentiality agreement shall contain terms substantially similar to the terms set forth in this Section 22. Each Bank and the Administrative Agent agree, unless specifically prohibited by applicable law or court order, to notify the Company of any request for disclosure of any such non-public information (x) by any governmental authority or representative thereof (other than any such request in connection with an examination of the financial condition of the Company by such governmental authority) or (y) pursuant to legal process. The obligations under this Section 22 shall survive for two (2) years after termination of this Agreement.

(b) This Agreement is intended to provide express authorization to each of the Banks and their Affiliates (and each employee, representative, or other agent of each Bank and its respective Affiliates) to disclose to any and all Persons, without limitation of any kind, the “tax treatment” and “tax structure” (in each case, within the meaning of Treasury Regulation Section 1.6011-4) of the transactions contemplated hereby and all materials of any kind (including opinions or other tax analyses) that are provided to the Banks or any of their Affiliates (and any such employees, representatives or other agents) relating to such tax treatment and structure; provided, that, with respect to any document or similar item that in either case contains information concerning the tax treatment or tax structure of the transactions contemplated hereby as well as other information, this authorization shall only apply to such portions of the documents or similar item that relate to the tax treatment or tax structure of the transactions contemplated hereby.

Section 23. *Severability*. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

Section 24. *Governing Law; Consent to Jurisdiction*. (a) This Agreement shall be governed by, and construed in accordance with, the laws of the State of New York.

(b) Each party hereto submits to the nonexclusive jurisdiction of the Supreme Court of the State of New York sitting in New York County and of the United States District Court of the Southern District of New York, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or for recognition or enforcement of any judgment, and each party hereto hereby agrees, to the fullest extent permitted by law, that all claims in respect of any such action or proceeding may be heard and determined in such New York State or, to the extent permitted by law, in such Federal court. Nothing in this Agreement shall affect any right that any party hereto may otherwise have to bring action or proceeding relating to this Agreement in the courts of any jurisdiction.

Section 25. *Headings*. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 26. *Counterparts; Integration*. This Agreement may be signed in any number of counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument. This Agreement, the Fee Letter, that certain Commitment Agreement dated as of March 17, 2010 between JPMorgan, J.P. Morgan Securities Inc., Union Bank, N.A., and the Company, that certain Letter Agreement between the Issuing Bank and the Company dated as of April 16, 2010 constitute the entire agreement and understanding among the parties hereto and, subject to Section 3(c), supersede any and all prior agreements and understandings, oral or written, relating to the subject matter hereof.

Section 27. *WAIVER OF JURY TRIAL*. TO THE EXTENT ALLOWED BY LAW, EACH OF THE COMPANY, THE BANKS AND THE ADMINISTRATIVE AGENT HEREBY IRREVOCABLY WAIVES ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY.

Section 28. *No Advisory or Fiduciary Responsibility*. In connection with all aspects of each transaction contemplated hereby (including in connection with any amendment, waiver or other modification hereof or any syndication of the credit facility provided hereunder), the Company acknowledges and agrees that: (i) (A) the arranging and other services regarding this Agreement provided by the Administrative Agent are arm's-length commercial transactions between the Company and its Affiliates, on the one hand, and the Administrative Agent and its Affiliates, on the other hand, (B) it has consulted its own legal, accounting, regulatory and tax advisors to the extent it has deemed appropriate, and (C) it is capable of evaluating, and understands and accepts, the terms, risks and conditions of the transactions contemplated hereby; (ii) (A) the Administrative Agent and the Company each is and has been acting solely as a principal and, except as expressly agreed in writing by the relevant parties, has not been, is not, and will not be acting as an advisor, agent or fiduciary for any other party hereto, any Affiliates of any other party hereto, or any other Person and (B) none of the Administrative Agent or the Company has any obligation to each other or to their respective Affiliates with respect to the transactions contemplated hereby except those obligations expressly set forth herein; and (iii) the Administrative Agent and its Affiliates may be engaged in a broad range of transactions that involve interests that differ from those of the Company and its Affiliates, and the Administrative Agent has no obligation to disclose any of such interests to the Company or its Affiliates. To the

fullest extent permitted by law, the Administrative Agent and the Company hereby waive and release any claims that they may have against each other with respect to any breach or alleged breach of agency or fiduciary duty in connection with any aspect of any transaction contemplated hereby. Each of the Administrative Agent and the Banks acknowledge and agree that it has consulted its own legal, accounting, regulatory and tax advisors to the extent it has deemed appropriate.

Section 29. *Waiver of Damages*. To the extent allowed by law, no party hereto shall have any liability with respect to, and each party hereto hereby waives, releases and agrees not to sue for, any special, indirect, consequential or punitive damages or losses suffered by such party in connection with, arising out of, or in any way related to this Agreement, the Letter of Credit or the transactions contemplated hereby or thereby regardless of whether such party shall have been advised of the possibility of such damages or losses or of the form of action in which such damages or losses may be claimed.

Section 30. *Government Regulations*. The Company agrees to provide documentary and other evidence of the Company's identity as may be requested by any Bank at any time to enable such Bank to verify the Company's identity or to comply with any applicable law or regulation, including, without limitation, Section 326 of the USA Patriot Act of 2001, 31 U.S.C. Section 5318.

Signature Pages Follow

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By: /s/ James R. Hatfield
Name: James R. Hatfield
Title: Senior Vice President and Chief Financial Officer

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent, Issuing Bank and as a Bank

By: /s/ Nancy R. Barwig
Name: Nancy R. Barwig
Title: Vice President

UNION BANK, N.A., as a Bank

By: /s/ Pascal Uttinger
Name: Pascal Uttinger
Title: Vice President

SCHEDULE I

The "**Letter of Credit Commission Rate**" and the "**Base Rate Margin**" for any day is the rate set forth below (in basis points per annum) under the column corresponding to the Status that exists on such day:

Status	Level I	Level II	Level III	Level IV	Level V
Base Rate Margin	100.0	150.0	175.0	200.0	250.0
Letter of Credit Commission Rate	200.0	250.0	275.0	300.0	350.0

For purposes of this Schedule, the following terms have the following meanings:

"**Level I Status**" exists at any date if, at such date, the higher of the two Ratings is:

A- or higher by S&P or A3 or higher by Moody's.

"**Level II Status**" exists at any date if, at such date, (i) Level I Status does not exist and (ii) the higher of the two Ratings is:

BBB+ or higher by S&P or Baa1 or higher by Moody's.

"**Level III Status**" exists at any date if, at such date, (i) neither Level I Status nor Level II Status exists and (ii) the higher of the two Ratings is:

BBB or higher by S&P or Baa2 or higher by Moody's.

"**Level IV Status**" exists at any date if, at such date, (i) none of Level I Status, Level II Status and Level III Status exists and (ii) the higher of the two Ratings is:

BBB- or higher by S&P or Baa3 or higher by Moody's.

"**Level V Status**" exists at any date if, at such date, no other Status exists.

"**Moody's**" means Moody's Investors Service, Inc., and any successor thereto.

"**Rating Agencies**" means Moody's and S&P.

"**Ratings**" means the credit ratings assigned to the senior unsecured long-term debt securities of the Company without third-party credit enhancement by the Rating Agencies. If there is no rating assigned to debt securities, the corporate credit rating will be used; and if Moody's or S&P shall not have in effect any rating assigned to senior unsecured long-term debt securities of the Company or corporate credit rating (other than by circumstances referred to in the last sentence of this definition), then such Rating Agency shall be deemed to have established

a Rating in Level V. Any rating assigned to any other debt security of the Company shall be disregarded. The rating in effect at any date is that in effect at the close of business on such date. In the case of split ratings from S&P or Moody's, the rating to be used to determine which pricing level applies is the higher of the two (e.g., BBB+/Baa2 results in Level II Status); provided that if the split is more than one full rating category, the rating category next below that of the higher of the two rating categories will be used (e.g., BBB+/Baa3 results in Level III Status, and A-/Baa3 results in Level II Status). If the rating system of Moody's or S&P shall change, or if either such Rating Agency shall cease to be in the business of rating corporate debt obligations, the Company, the Administrative Agent and the Banks shall negotiate in good faith to amend this definition to reflect such changed rating system or the unavailability of ratings from such Rating Agency and, pending the effectiveness of any such amendment, the Letter of Credit Commission Rate and the Base Rate Margin shall be determined by reference to the Rating most recently in effect prior to such change or cessation.

"**S&P**" means Standard & Poor's Financial Services LLC, a division of The McGraw-Hill Companies, Inc., and any successor thereto.

"**Status**" refers to the determination of which of Level I Status, Level II Status, Level III Status, Level IV Status or Level V Status exists at any date.

SCHEDULE II

Bank	Participation Percentage	Participation Amount
JPMorgan Chase Bank, N.A.	51.46682890154%	$ 17,753,152.95
Union Bank, N.A.	48.53317109846%	$ 16,741,206.49

EXHIBIT A

AMENDED AND RESTATED
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. P-010152
(formerly numbered as S-1002)

Originally Issued August 18, 1986
Amended and Restated
April 16, 2010

Emerson Finance LLC
8000 W. Florissant Avenue
P.O. Box 4100
St. Louis, Missouri 63136

Attention: President

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "**Company**"), in your favor, our Irrevocable Transferable Letter of Credit No. P-010152 (formerly numbered as S-1002) (the "**Letter of Credit**"), in a maximum amount at any date (the "**Maximum Credit Amount**") equal to the amount shown opposite the period including such date in the Table of Maximum Credit Amounts attached hereto as Schedule II-A, effective immediately and expiring at 5:00 p.m. (New York City time) on the Termination Date. Capitalized terms used herein and in Schedules II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "**Facility Lease**") as amended and in effect on the date hereof, between the Company and U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston), as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "**Date of Drawing**") in the Table of Maximum Drawing Amounts attached hereto as Schedule II-B as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next paragraph, are hereinafter referred to collectively as the "**Maximum Drawing Amounts**" and individually as the "**Maximum Drawing Amount**". A drawing in respect of a payment hereunder honored by us shall not exceed the lesser of the Maximum Drawing Amount applicable on the Date of Drawing and the Maximum Credit Amount applicable on the Date of Drawing. All payments hereunder shall be made from our own general funds.

The Maximum Drawing Amounts shall be modified from time to time as follows:

(a) upon payment by the Issuing Bank of each drawing under the Letter of Credit, the Maximum Drawing Amounts applicable to each Date of Drawing subsequent to such payment shall be automatically reduced by an amount equal to the amount of the drawing so paid and shall not be reinstated; and

(b) if adjustments are made to Modified Special Casualty Values, corresponding adjustments shall be made to the Maximum Drawing Amounts shown in Schedule II-B, (as theretofore reduced pursuant to clause (a) above), *provided* that if any such adjustment of Modified Special Casualty Values would cause the Maximum Drawing Amount for any period to exceed the Maximum Credit Amount for such period, (minus, the amount of any drawing theretofore honored by us hereunder), such Maximum Credit Amount (as so reduced) shall apply for such period and *provided further* that adjustments pursuant to this clause (b) shall be effective automatically upon receipt by us of a notice from you in the form of Exhibit 1 hereto.

Upon receipt of a notice in the form of Exhibit 1 hereto, we will promptly issue an amendment to this irrevocable transferable letter of credit containing a revised Schedule II-B reflecting the adjustments contained in such notice.

Funds under this Letter of Credit are available to you against presentation on or prior to the Termination Date of your drawing in the form of a completed certificate signed by you in the form of Exhibit 2 attached hereto. Such certificate shall be dated the date of its presentation and shall be presented (x) by facsimile (at facsimile number (312) 233-2266 or alternately to (312) 954-2458), Attention: Manager, without further need of documentation, including the original of this Letter of Credit, or (y) at our Chicago office specified below, in each case, it being understood that each certificate so submitted is to be the sole operative instrument of drawing. You shall use your best efforts to give telephonic notice of a drawing to the Issuing Bank at its Standby Service Unit, (at: (312) 954-5973 or alternately to 1-800-634-1969, Option 1) on the day of such drawing (but such notice shall not be a condition to drawing hereunder and you shall have no liability for not doing so). If we receive such certificate as provided herein, in strict conformity with the terms and conditions of this Letter of Credit, prior to 10:00 a.m. (New York City time) on any Business Day, (notwithstanding any provision of Rule 5.01 of the International Standby Practices, ICC Publication No. 590 (the "**ISP98**") to the contrary, which provisions of the ISP98 are hereby expressly waived), we will honor the drawing on the same Business Day. If we receive such certificate as provided herein on or after 10:00 a.m. and prior to 5:00 p.m. (New York City time) on any Business Day, all in strict conformity with the terms and conditions of this Letter of Credit, we will honor the drawing on the next Business Day. Payment under this Letter of Credit will be made by wire transfer of federal funds to your account with any bank located in the United States of America or by deposit of immediately available funds into a designated account that you maintain with us.

Notwithstanding any provision of Section 5-108(b) of the New York Uniform Commercial Code (the "**NY UCC**") or Rule 5.01 of the ISP98 to the contrary, which provisions are hereby expressly waived, if the presentation of such certificate is not in strict conformity with the terms and conditions of this Letter of Credit, we will give you prompt notice prior to the time we would have been obliged to make payment as set forth in the preceding paragraph by

facsimile transmission addressed to you at the fax number set forth in the next succeeding paragraph, effective upon confirmation, that we have refused such non-conforming certificate, and stating all discrepancies in respect of which the Issuing Bank refuses such non-conforming certificate. If you correct such non-conforming demand by presentation of the certificate corrected to be in strict conformity with the terms and conditions of the Letter of Credit, then we will honor the drawing and make payment in accordance with the terms provided herein based upon the time such corrected certificate is presented, *provided* that you may make only one such corrected demand with respect to any such non-conforming demand, and *provided further* that any such correction and presentation of such conforming demand is effected on or prior to the Stated Termination Date, and *provided further* that for purposes of determining whether such certificate has been timely presented, the corrected certificate shall be deemed to have been presented on the date the non-conforming certificate was presented.

Notwithstanding any other provision of this Letter of Credit, we shall have the right, upon the occurrence of any of the events listed in Schedule III hereto, to terminate this Letter of Credit by delivering to you a written notice in the form of Exhibit 4 hereto indicating the date of such termination (the "**Date of Early Termination**"), *provided* that on or before the Date of Early Termination you will have the right to draw once an amount not in excess of the lesser of the Maximum Credit Amount and the Maximum Drawing Amount in accordance with the procedures described herein. The written notice referred to in the preceding sentence shall be given by facsimile transmission addressed to you at Emerson Finance LLC, 8000 W. Florissant Avenue, P.O. Box 4100, St. Louis, Missouri 63136; Attention: President; Fax: 314-553-2463 (or to such other address or facsimile number designated by you by written notice delivered to us at least 15 days prior to the notice of early termination) and shall be effective upon receipt of the appropriate confirmation of the facsimile transmission. We will also forward a copy of such notice by overnight delivery service to the address set forth above. The Date of Early Termination specified in such written notice shall be:

(a) in the case of events specified in paragraphs A and G of Schedule III, not earlier than ten days after such notice is given, and

(b) in the case of all other events specified in Schedule III, not earlier than 30 days after such notice is given.

Upon the Termination Date this Letter of Credit shall automatically terminate and be delivered to the Issuing Bank for cancellation. Failure to deliver said Letter of Credit will have no effect on the Termination Date, and the Letter of Credit will still be considered terminated.

Notwithstanding the provisions of Section 5-112(b)(2) of the NY UCC that permit the Issuing Bank to refuse to recognize or carry out a transfer of this Letter of Credit if the transferee has failed to comply with any other requirement relating to transfer imposed by the Issuing Bank which is within the standard practice referred to in Section 5-108(e) of the NY UCC or is otherwise reasonable under the circumstances, which provisions are hereby expressly waived, this Letter of Credit may be transferred in its entirety more than once, but in each case only to the successor Equity Participant under the Trust Agreement dated as of August 1, 1986 between yourself and U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston). Any transfer request must be

effected by presenting to the Issuing Bank the attached form of Exhibit 3 hereto signed by the transferor and by the transferee accompanied by the original of this Letter of Credit and any amendments thereto (which presentation of an appropriately completed Exhibit 3 shall be conclusive evidence of such transferee's authority without any inquiry by us into the terms of the Trust Agreement). Upon the Issuing Bank's endorsement of such transfer, the transferee instead of the transferor shall, without necessity of further action, be entitled to all the benefits of and rights under this Letter of Credit in the transferor's place.

Notwithstanding any provision of Rule 3.12 of the ISP98 to the contrary, which provisions are hereby expressly waived, upon the Issuing Bank's receipt of its standard certificate duly executed by you certifying that the original of this Letter of Credit has been lost, destroyed or mutilated, the Issuing Bank shall provide a true copy of original (which copy shall be marked as such) of this Letter of Credit to you without affecting the Company's obligations to the Issuing Bank to reimburse. Upon delivery of such copy, any requirement that the original be presented hereunder shall be deemed to be a reference to such copy.

Except as expressly stated herein, this Letter of Credit is governed by, and construed in accordance with the ISP98. As to matters not governed by the ISP98, this Letter of Credit shall be governed by and construed in accordance with the laws of the State of New York, including without limitation the NY UCC as in effect in the State of New York, without regard to principles of conflict of laws (other than Sections 5.1401 and 5.1402 of the General Obligations Law of the State of New York).

Communications with respect to this Letter of Credit shall be in writing, specifically referring to the number of this Letter of Credit, and addressed and presented to the Issuing Bank at JPMorgan Chase Bank, N.A., 300 South Riverside Plaza, Mail Code IL1-0236, Chicago, Il 60606-0236, Attention: Standby Letter of Credit Unit. For telephone assistance, please contact the Standby Client Service Unit at 1-800-634-1969, select Option 1, and have this Letter of Credit number available.

By your acceptance of this Letter of Credit, we hereby notify you of our agreement to the terms and conditions of Section 13 of the Reimbursement Agreement.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein, except only Schedules I, II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto and the notices referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except as set forth above.

This Letter of Credit No. P-010152 (formerly numbered as S-1002) amends and restates our Letter of Credit No. S-1002 dated as of August 15, 1986, as heretofore amended.

JPMORGAN CHASE BANK, N.A.

By: _____
Name:
Title:

EXHIBIT 1
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236

Attn: Standby Letter of Credit Unit

Dear Sirs:

Reference is made to that certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010152 (formerly numbered as S-1002) dated April 16, 2010 (the "**Letter of Credit**"), which has been established by you in favor of Emerson Finance LLC (the "**Equity Participant**").

The undersigned, a duly authorized representative of the Equity Participant, hereby certifies that Modified Special Casualty Values have been adjusted and the amounts shown on Schedule II-B to the Letter of Credit should be modified, in accordance with the terms of clauses (a) and (b) of the third paragraph of the Letter of Credit, to the amounts shown in Appendix A hereto.

We request that you amend the Letter of Credit to replace the current Schedule II-B to the Letter of Credit with the revised Schedule II-B attached hereto. All other terms and conditions as stated in the Letter of Credit will remain unchanged. Except as otherwise set forth herein, the Letter of Credit shall remain effective and in full force.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

_____
[Name of Equity Participant**]**

_____
[Name and Title of Authorized

_____
Representative of Equity Participant**]**

EXHIBIT 2
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

CERTIFICATE

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236
Attn: Standby Letter of Credit Unit
Facsimile number (312) 233-2266
Alternately to (312) 954-2458

The undersigned, a duly authorized representative of Emerson Finance LLC (the "**Equity Participant**"), as beneficiary under that certain amended and restated irrevocable transferable Letter of Credit No. P-010152 (formerly numbered as S-1002) dated April 16, 2010, established by JPMorgan Chase Bank, N.A. (the "**Issuing Bank**") and issued pursuant to that certain Reimbursement Agreement dated as of April 16, 2010 between Arizona Public Service Company (the "**Company**"), the Issuing Bank and the other Banks named therein, hereby certifies as follows:

1. We hereby demand payment in the amount of $_____.

2. An Event of Default under the Facility Lease has occurred and is continuing.

3. The amount demanded hereby does not exceed the Maximum Drawing Amount available under the Letter of Credit on the date hereof, as determined in accordance with the terms of the Letter of Credit.

4. Payment by the Issuing Bank pursuant to this drawing shall be made to _____, ABA Number _____, Account Number _____, Attention: _____, Re: _____.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed this Certificate as of _____, 20_____.

_____
[Name of Equity Participant**]**

[Name and Title of Authorized
Representative of Equity Participant**]**

EXHIBIT 3
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

REQUEST FOR TRANSFER

JPMorgan Chase Bank, N.A.
300 South Riverside Plaza
Mail Code IL1-0236
Chicago, IL 60606-0236

[Date]

Attn: Standby Letter of Credit Unit

Re: JPMorgan Chase Bank, N.A. Irrevocable Transferable Letter of Credit No. P-010152 (formerly numbered as S-1002) dated April 16, 2010.

We, the undersigned "Transferor", hereby irrevocably transfer all of our rights to draw under the above referenced Letter of Credit ("Credit") in its entirety to:

NAME OF TRANSFEREE _____
(Print Name and complete address of the Transferee) "Transferee"

ADDRESS OF TRANSFEREE _____

_____

CITY, STATE/COUNTRY ZIP _____

In accordance with ISP98 (as defined in the Credit), Rule 6, regarding transfer of drawing rights, all rights of the undersigned Transferor in such Credit are transferred to the Transferee, who shall have the sole rights as beneficiary thereof, including sole rights relating to any amendments whether increases or extensions or other amendments and whether now existing or hereafter made. All amendments are to be advised directly to the Transferee without necessity of any consent of or notice to the undersigned Transferor.

The original Credit, including amendments to this date, is attached and the undersigned Transferor requests that you endorse an acknowledgment of this transfer on the reverse thereof. The undersigned Transferor requests that you notify the Transferee of this Credit in such form and manner as you deem appropriate, and the terms and conditions of the Credit as transferred. The undersigned Transferor acknowledges that you incur no obligation to process the transfer requested hereunder if the transfer is to a prohibited person named by the United States Department of Treasury's Office of Foreign Assets Control Regulations.

The Transferor and the Transferee hereby request that you advise the Transferee of the terms and conditions of this transferred Credit and these instructions.

In the event that the authorized signatory for either the Transferor or the Transferee is a financial institution, a corporation or a partnership composed of financial institutions or corporations, a secretary or incumbency certificate certifying that such signatory is duly empowered to act in the name and on behalf of such Transferor or Transferee, as applicable, must accompany this

Request for Transfer, and, in such case, the requirement that such signatory's signature be guaranteed shall be deemed to be waived.

Payment of transfer fee of U.S. $3,500 is for the account of the Company (as defined in the Credit) who agrees to pay you on demand any expense or cost you may incur in connection with the transfer. Receipt of such transfer fee shall not constitute consent to effect the transfer of the Credit on terms other than as expressly set forth in the Credit and this Request for Transfer.

Transferor represents and warrants to you that (i) our execution, delivery, and performance of this request for transfer (a) are within our powers, (b) have been duly authorized, (c) constitute our legal, valid, binding and enforceable obligation, (d) do not contravene any charter provision, by-law, resolution, contract, or other undertaking binding on or affecting us or any of our properties, (e) to the best of Transferor's knowledge, such transfer does not require any notice, filing or other action to, with, or by any governmental authority, (f) the enclosed Credit is original and complete, (g) there is no outstanding demand or request for payment or transfer under the Credit affecting the rights to be transferred which remains outstanding as of the date hereof, (h) in the event that the Transferee's signature is not guaranteed, to the best of Transferor's knowledge, the Transferee is a financial institution, a corporation or a partnership composed of financial institutions or corporations and (i) to the best of Transferor's knowledge, based on information provided by the Transferee, the Transferee's name and address are correct and complete and the Transferee's use of the Credit as transferred and the transactions underlying the Credit and the requested transfer do not violate any applicable United States or other law, rule or regulation.

The effective date of the transfer shall be the date hereafter on which you effect the requested transfer by acknowledging and endorsing this request and giving notice thereof to Transferee.

WE WAIVE ANY RIGHT TO TRIAL BY JURY THAT WE MAY HAVE IN ANY ACTION OR PROCEEDING RELATING TO OR ARISING OUT OF THIS TRANSFER.

This request is made subject to ISP98 and is subject to and shall be governed by the laws of the State of New York, without regard to principles of conflict of laws.

Sincerely yours,

_____
(Print Name of Transferor)

_____
(Transferor's Authorized Signature)

_____
(Print Authorized Signers Name and Title)

SIGNATURE GUARANTEED

Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement. We attest that the individual, company or entity has been identified by us in compliance with USA PATRIOT Act procedures of our bank.

_____
(Print Name of Bank)

_____
(Address of Bank)

_____
(City, State, Zip Code)

_____
(Print Name and Title of Authorized Signer)

_____
(Authorized Signature)

_____
(Telephone Number)

_____
(Date)

(Telephone Number/Fax Number)

Acknowledged:

(Print Name of Transferee)

(Transferee's Authorized Signature)

(Print Authorized Signers Name and Title)

(Telephone Number/Fax Number)

Acknowledged as of _____, 20_____:

JPMorgan Chase Bank, N.A.

By: _____
Name:
Title:

SIGNATURE GUARANTEED

Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement. We attest that the individual, company or entity has been identified by us in compliance with USA PATRIOT Act procedures of our bank.

(Print Name of Bank)

(Address of Bank)

(City, State, Zip Code)

(Print Name and Title of Authorized Signer)

(Authorized Signature)

(Telephone Number)

(Date)

EXHIBIT 4
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

NOTICE OF TERMINATION

Date: _____ __, 20__

Emerson Finance LLC
8000 W. Florissant Avenue
P.O. Box 4100
St. Louis, Missouri 63136

Attention: President

Dear Sir:

Reference is made to that certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010152 (formerly numbered as S-1002) dated April 16, 2010, which has been established by us in your favor.

We hereby give notice to you that the above referenced Letter of Credit will be terminated in accordance with its terms on _____ _____, 20_____, pursuant to the occurrence of one or more of the events described in Schedule III to the Letter of Credit as follows:

[Insert the description of the event(s) of default**]**

Very truly yours,

JPMORGAN CHASE BANK, N.A.

By: _____
Name:
Title:

SCHEDULE I
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

The following terms have the following meanings for purposes of the Letter of Credit and the Schedules and Exhibits thereto. Terms defined in the Letter of Credit have the meanings given to them therein. Terms defined by reference to the Facility Lease have the meanings assigned to them therein from time to time.

"**Administrative Agent**" means JPMorgan, in its capacity as administrative agent for the Banks under the Reimbursement Agreement, and its successors in such capacity.

"**Applicable Law**" has the meaning assigned to it in the Facility Lease.

"**Bank**" means (i) each bank or financial institution listed on the signature pages of the Reimbursement Agreement, each Assignee that becomes a Bank pursuant to Section 15(a) of the Reimbursement Agreement, and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"**Business Day**" means any day except (i) a Saturday or Sunday, (ii) any other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close, or (iii) a day on which payments in respect of the Letter of Credit cannot be funded via wire through the Federal Reserve System.

"**Capital Lease Obligations**" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are required to be classified and accounted for as a capital lease on the balance sheet of such Person under generally accepted accounting principles and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with generally accepted accounting principles.

"**Code**" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"**Debtor Relief Laws**" means the Bankruptcy Code of the United States, and all other liquidation, conservatorship, bankruptcy, assignment for the benefit of creditors, moratorium, rearrangement, receivership, insolvency, reorganization, or similar debtor relief laws of the United States or other applicable jurisdictions from time to time in effect and affecting the rights of creditors generally.

"**Defaulting Bank**" means any Bank, as reasonably determined by the Administrative Agent or if the Administrative Agent is the Defaulting Bank, by the Required Banks, that (a) has defaulted in its obligation to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement, (b) has notified the Company, the Administrative Agent, the Issuing Bank or any Bank in writing of its intention not to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement, (c) has otherwise failed to pay over to the Administrative Agent or any other Bank any other amount required to be paid by it thereunder within three (3) Business Days of the date when due, (d) has failed, within three (3) Business Days after request by the Administrative Agent, or if the

Administrative Agent is the Defaulting Bank, by the Required Banks, to confirm that it will comply with the terms of the Reimbursement Agreement relating to its obligations to fund its Participation Percentage in respect of a drawing under the Letter of Credit or any of its other funding obligations under the Reimbursement Agreement or (e) shall (or whose parent company shall) generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or shall have had any proceeding instituted by or against such Bank (or its parent company) seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for, it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 30 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, administrator, assignee for the benefit of creditors or similar Person charged with reorganization or liquidation of its business or custodian for it or for any substantial part of its property) shall occur, or shall take (or whose parent company shall take) any corporate action to authorize any of the actions set forth above in this clause (e); provided that a Bank shall not be deemed to be a Defaulting Bank solely by virtue of the ownership or assumption of any equity interest in any Bank or any Person that directly or indirectly controls such Bank by a governmental authority or an instrumentality thereof.

"**Equity Participant**" means Emerson Finance LLC, as Equity Participant, and its successors and assigns.

"**ERISA**" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"**ERISA Affiliate**" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"**Governmental Action**" has the meaning assigned to it in the Facility Lease.

"**Guarantee**" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), *provided* that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "Guarantee" used as a verb has a corresponding meaning.

"**Hedge Agreement**" means any interest rate swap, cap or collar agreement, interest rate future or option contract, currency swap agreement, currency future or option contract, commodity future or option contract, commodity forward contract or other similar agreement.

"**Indebtedness**" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"**Issuing Bank**" means JPMorgan and its successors in their capacity as issuer of the Letter of Credit.

"**JPMorgan**" means JPMorgan Chase Bank, N.A., a national banking association, in its individual capacity, and its successors and assigns.

"**Material Subsidiary**" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of April 16, 2010 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"**Modified Special Casualty Value**" has the meaning assigned to it in the Facility Lease.

"**Multiemployer Plan**" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"**Participant**" has the meaning set forth in Section 15(b) of the Reimbursement Agreement.

"**Participation**" means a participating interest in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a) of the Reimbursement Agreement, but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b) of the Reimbursement Agreement.

"**Participation Amount**" means, with respect to any Bank, the amount set forth in Schedule II to the Reimbursement Agreement opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"**Participation Percentage**" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"**PBGC**" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"**Person**" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"**Plan**" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"**Reimbursement Agreement**" means the Reimbursement Agreement dated as of April 16, 2010 among Arizona Public Service Company, the Banks party thereto, the Administrative Agent and the Issuing Bank, and as the same may be amended and restated from time to time thereafter.

"**Required Banks**" means, at any time, Banks with Participation Percentages aggregating more than 50% at such time exclusive of any Defaulting Bank; provided that if after application of such provision, any Bank shall hold more than 50% of the aggregate Participation Percentages of all Banks at such time (and if there is more than one Bank at such time), "Required Banks" shall mean such Bank plus one additional Bank.

"**Stated Termination Date**" means April 16, 2013 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17 of the Reimbursement Agreement.

"**Subsidiary**" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

"**Termination Date**" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), (v) the date on which the Company delivers a certificate to the Issuing Bank

certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected certificate in strict conformity with the terms and conditions of the Letter of Credit is presented on such date as specified in, and in accordance with the provisions of, the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the drawing in accordance with the provisions of such paragraph pursuant to such presentation.

"**Transaction Documents**" means the Participation Agreement, the Refinancing Agreement, the Indemnity Agreement, the Escrow Deposit Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents, any ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement and the Notes, each as defined in the Facility Lease.

"**Voting Stock**" means capital stock issued by a corporation, or equivalent interests in any other Person, the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of directors (or persons performing similar functions) of such Person, even if the right so to vote has been suspended by the happening of such a contingency.

SCHEDULE II-A
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

TABLE OF MAXIMUM CREDIT AMOUNTS
EMERSON FINANCE LLC

APPLICABLE PERIOD	MAXIMUM CREDIT AMOUNT
From April 16, 2010 through July 10, 2010	$ 34,494,359.44
From July 11, 2010 through January 10, 2011	$ 33,579,978.69
From January 11, 2011 through July 10, 2011	$ 30,797,976.57
From July 11, 2011 through January 10, 2012	$ 28,422,763.42
From January 11,2012 through July 10, 2012	$ 25,438,865.48
From July 11, 2012 through January 10, 2013	$ 23,024,963.77
From January 11, 2013 through April 16, 2013	$ 19,942,099.63

SCHEDULE II-B
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

TABLE OF MAXIMUM DRAWING AMOUNTS
EMERSON FINANCE LLC

APPLICABLE PERIOD	MAXIMUM DRAWING AMOUNT
From April 16, 2010 through July 10, 2010	$ 34,494,359.44
From July 11, 2010 through January 10, 2011	$ 33,579,978.69
From January 11, 2011 through July 10, 2011	$ 30,797,976.57
From July 11, 2011 through January 10, 2012	$ 28,422,763.42
From January 11,2012 through July 10, 2012	$ 25,438,865.48
From July 11, 2012 through January 10, 2013	$ 23,024,963.77
From January 11, 2013 through April 16, 2013	$ 19,942,099.63

SCHEDULE III
TO JPMORGAN CHASE BANK, N.A. LETTER OF CREDIT NO. P-010152

The Issuing Bank shall have the right upon the occurrence of any of the events listed below to terminate the Letter of Credit in accordance with the terms of the Letter of Credit:

(A) The Company shall fail to pay when due any amount payable under Section 2(a) of the Reimbursement Agreement or fail to pay any other amount payable under Section 2 of the Reimbursement Agreement within five (5) Business Days after the same becomes due and payable; or

(B) The Company shall fail to perform or observe (i) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 8(a), 8(b), 8(c) or 8(e) of the Reimbursement Agreement, or (ii) any term, covenant or agreement contained in the Reimbursement Agreement (other than those covered by clause (A) above or subclause (i) of this clause (B) or Section 7(e) or Section 19 of the Reimbursement Agreement) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(C) Any representation or warranty made by the Company in the Reimbursement Agreement or by the Company (or any of its officers) in any certificate delivered in connection with the Reimbursement Agreement shall prove to have been false or misleading in any material respect when made; or

(D) Any material provision of the Reimbursement Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under the Reimbursement Agreement; or

(E) (i) The Company or any of its Material Subsidiaries shall fail to pay (a) any principal of or premium or interest on any Indebtedness that is outstanding in a principal amount of at least $35,000,000 in the aggregate (but excluding Indebtedness owing under the Reimbursement Agreement), or (b) an amount, or post collateral as contractually required in an amount, of at least $35,000,000 in respect of any Hedge Agreement, of the Company or such Material Subsidiary (as the case may be), in each case, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness or Hedge Agreement; or (ii) any event of default shall exist under any agreement or instrument relating to any such Indebtedness and shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such event is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(F) The Company or any of its Material Subsidiaries shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least $35,000,000, when the same

becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(G) The Company or any of its Material Subsidiaries shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company or any of its Material Subsidiaries seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any Debtor Relief Law, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company or any of its Material Subsidiaries shall take any corporate action to authorize any of the actions set forth above in this clause (G); or

(H) Judgments or orders for the payment of money that exceeds any applicable insurance coverage (the insurer of which shall be rated at least "A" by A.M. Best Company) by more than $35,000,000 in the aggregate shall be rendered against the Company or any Material Subsidiary and such judgments or orders shall continue unsatisfied or unstayed for a period of 45 days; or

(I) (i) Any "person" or "group" (as such terms are used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended, but excluding any employee benefit plan of such person or its subsidiaries, and any person or entity acting in its capacity as trustee, agent or other fiduciary or administrator of any such plan) becomes the "beneficial owner" (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, as amended), directly or indirectly, of 30% or more of the equity securities of PWCC entitled to vote for members of the board of directors of PWCC; or (ii) during any period of 24 consecutive months, a majority of the members of the board of directors of PWCC cease (other than due to death or disability) to be composed of individuals (a) who were members of that board on the first day of such period, (b) whose election or nomination to that board was approved by individuals referred to in clause (a) above constituting at the time of such election or nomination at least a majority of that board or (c) whose election or nomination to that board was approved by individuals referred to in clauses (a) and (b) above constituting at the time of such election or nomination at least a majority of that board; or (iii) PWCC shall cease for any reason to own, directly or indirectly 80% of the Voting Stock of the Company; or

(J) An event or condition specified in Section 7(g)(iv) of the Reimbursement Agreement shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the

foregoing) which is, in the determination of the Required Banks, likely to exceed $35,000,000 in the aggregate; or

(K) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(L) any event specified in subsection (vii), (viii) or (x) of Section 15 of the Facility Lease shall occur; or

(M) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding $1,000,000 within the periods specified in that Section.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit. This Letter of Credit No. P-010152 (formerly numbered as S-1002) amends and restates our Letter of Credit No. S-1002 dated as of August 15, 1986, as heretofore amended.

EXHIBIT B

FORM OF ASSIGNMENT AND ASSUMPTION AGREEMENT

This Assignment and Assumption Agreement (the "Assignment and Assumption") is dated as of the Effective Date set forth below and is entered into by and between **[***Insert name of Assignor***]** (the "Assignor") and **[***Insert name of Assignee***]** (the "Assignee"). Capitalized terms used herein or in Annex 1 hereto but not defined herein or therein shall have the meanings given to them in the Reimbursement Agreement identified below (as amended, the "Reimbursement Agreement"), receipt of a copy of which is hereby acknowledged by the Assignee. The Terms and Conditions set forth in Annex 1 attached hereto are hereby agreed to and incorporated herein by reference and made a part of this Assignment and Assumption as if set forth herein in full.

For an agreed consideration, the Assignor hereby irrevocably sells and assigns to the Assignee, and the Assignee hereby irrevocably purchases and assumes from the Assignor, subject to and in accordance with the Terms and Conditions and the Reimbursement Agreement, as of the Effective Date inserted by the Administrative Agent as contemplated below, the interest in and to all of the Assignor's rights and obligations in its capacity as a Bank under the Reimbursement Agreement and any other documents or instruments delivered pursuant thereto that represents the amount and percentage interest identified below of all of the Assignor's outstanding rights and obligations under the respective facilities identified below (including without limitation any guaranties included in such facilities and, to the extent permitted to be assigned under applicable law, all claims (including without limitation contract claims, tort claims, malpractice claims, statutory claims and all other claims at law or in equity), suits, causes of action and any other right of the Assignor against any Person whether known or unknown arising under or in connection with the Reimbursement Agreement, any other documents or instruments delivered pursuant thereto or the loan transactions governed thereby) (the "Assigned Interest"). Such sale and assignment is without recourse to the Assignor and, except as expressly provided in this Assignment and Assumption, without representation or warranty by the Assignor.

1. Assignor: _____

2. Assignee: _____

[and is an Affiliate/Approved Fund of **[***identify Bank***]]**[1]

3. Company: Arizona Public Service Company

4. Administrative JPMorgan Chase Bank, N.A., as Administrative

1 Select as applicable.

Agent: Agent under the Reimbursement Agreement

5. Assignee: _____

6. Reimbursement Agreement: The Reimbursement Agreement dated as of April 16, 2010 among Arizona Public Service Company, the Banks party thereto, JPMorgan Chase Bank, N.A., as Issuing Bank and as Administrative Agent.

7. Assigned Interest:

Facility Assigned	Aggregate Amount of Participation Percentages/ Disbursement Advances for all Banks*	Amount of Participation Percentage/ Disbursement Advances Assigned*	Percentage Assigned of Participation Percentage / Aggregate Disbursement Advances[2]
Letter of Credit Facility	$	$	_____%

8. Trade Date: _____[3]

Effective Date: _____, 20_____ **[**TO BE INSERTED BY ADMINISTRATIVE AGENT AND WHICH SHALL BE THE EFFECTIVE DATE OF RECORDATION OF TRANSFER BY THE ADMINISTRATIVE AGENT.**]**

The terms set forth in this Assignment and Assumption are hereby agreed to:

ASSIGNOR

[NAME OF ASSIGNOR**]**

---

* Amount to be adjusted by the counterparties to take into account any payments or prepayments made between the Trade Date and the Effective Date.

2 Set forth, to at least 9 decimals, as a percentage of the Participation Percentages/Disbursement Advances of all Banks thereunder.

3 Insert if satisfaction of minimum amounts is to be determined as of the Trade Date.

By: _____
Title:

ASSIGNEE

[NAME OF ASSIGNEE]

By: _____
Title:

[Consented to and]4 Accepted:

JPMORGAN CHASE BANK, N.A., as
Administrative Agent

By: _____
Title:

[Consented to:]5

ARIZONA PUBLIC SERVICE COMPANY

By: _____
Title:

4 To be added only if the consent of the Administrative Agent is required by the Reimbursement Agreement.

5 To be added only if the consent of the Company is required by the terms of the Reimbursement Agreement.

ANNEX 1
TERMS AND CONDITIONS FOR
ASSIGNMENT AND ASSUMPTION

1. Representations and Warranties.

1.1 Assignor. The Assignor represents and warrants that (i) it is the legal and beneficial owner of the Assigned Interest, (ii) the Assigned Interest is free and clear of any lien, encumbrance or other adverse claim and (iii) it has full power and authority, and has taken all action necessary, to execute and deliver this Assignment and Assumption and to consummate the transactions contemplated hereby. Neither the Assignor nor any of its officers, directors, employees, agents or attorneys shall be responsible for (i) any statements, warranties or representations made in or in connection with the Reimbursement Agreement, (ii) the execution, legality, validity, enforceability, genuineness, sufficiency, perfection, priority, collectibility, or value of the Reimbursement Agreement, (iii) the financial condition of the Company, any of its Subsidiaries or Affiliates or any other Person obligated in respect of the Reimbursement Agreement, (iv) the performance or observance by the Company, any of its Subsidiaries or Affiliates or any other Person of any of their respective obligations under the Reimbursement Agreement, (v) inspecting any of the property, books or records of the Company, or any guarantor, or (vi) any mistake, error of judgment, or action taken or omitted to be taken in connection with the LC Disbursements or the Reimbursement Agreement.

1.2. Assignee. The Assignee (a) represents and warrants that (i) it has full power and authority, and has taken all action necessary, to execute and deliver this Assignment and Assumption and to consummate the transactions contemplated hereby and to become a Bank under the Reimbursement Agreement, (ii) from and after the Effective Date, it shall be bound by the provisions of the Reimbursement Agreement as a Bank thereunder and, to the extent of the Assigned Interest, shall have the obligations of a Bank thereunder, (iii) agrees that its payment instructions and notice instructions are as set forth in Schedule 1 to this Assignment and Assumption, (iv) confirms that none of the funds, monies, assets or other consideration being used to make the purchase and assumption hereunder are “plan assets” as defined under ERISA and that its rights, benefits and interests in and under the Reimbursement Agreement will not be “plan assets” under ERISA, (v) agrees to indemnify and hold the Assignor harmless against all losses, costs and expenses (including, without limitation, reasonable attorneys’ fees) and liabilities incurred by the Assignor in connection with or arising in any manner from the Assignee’s non-performance of the obligations assumed under this Assignment and Assumption, (vi) it has received a copy of the Reimbursement Agreement, together with copies of financial statements and such other documents and information as it has deemed appropriate to make its own credit analysis and decision to enter into this Assignment and Assumption and to purchase the Assigned Interest on the basis of which it has made such analysis and decision independently and without reliance on the Administrative Agent or any other Bank, and (vii) attached as Schedule 1 to this Assignment and Assumption is any documentation required to be delivered by the Assignee with respect to its tax status pursuant to the terms of the Reimbursement Agreement, duly completed and executed by the Assignee and (b) agrees that (i) it will, independently and without reliance on the Administrative Agent, the Assignor or any other

Bank, and based on such documents and information as it shall deem appropriate at the time, continue to make its own credit decisions in taking or not taking action under the Reimbursement Agreement, and (ii) it will perform in accordance with their terms all of the obligations which by the terms of the Reimbursement Agreement are required to be performed by it as a Bank.

2. Payments. The Assignee shall pay the Assignor, on the Effective Date, the amount agreed to by the Assignor and the Assignee. From and after the Effective Date, the Administrative Agent shall make all payments in respect of the Assigned Interest (including payments of principal, interest, fees and other amounts) to the Assignor for amounts which have accrued to but excluding the Effective Date and to the Assignee for amounts which have accrued from and after the Effective Date.

3. General Provisions. This Assignment and Assumption shall be binding upon, and inure to the benefit of, the parties hereto and their respective successors and assigns. This Assignment and Assumption may be executed in any number of counterparts, which together shall constitute one instrument. Delivery of an executed counterpart of a signature page of this Assignment and Assumption by telecopy shall be effective as delivery of a manually executed counterpart of this Assignment and Assumption. This Assignment and Assumption shall be governed by, and construed in accordance with, the law of the State of New York.

Exhibit 10.4

PINNACLE WEST
CAPITAL CORPORATION

Donald E. Brandt
Chairman and Chief Executive Officer

Tel 602/250-5602
Fax 602/250-3303

Mail Station 9042
PO Box 53999
Phoenix, AZ 85072-3999

May 21, 2009

Mr. David P Falck
403 Shelbourne Terrace
Ridgewood, NJ 07450

Dear Dave,

I am delighted to extend to you this offer to become the Executive Vice President, General Counsel and Secretary of both Pinnacle West Capital Corporation and Arizona Public Service Company. The details of our proposal are included in Attachment A.

If you are in agreement with the terms of our offer of employment as described herein, please sign as requested below.

Dave, I am confident that this will be a challenging and rewarding opportunity for you. I am excited about the prospect of you joining our team and we will do all we can to ensure a smooth transition for you and Sally. I look forward to your contributions to our organization.

If you have any questions, please do not hesitate to contact me.

Sincerely,

/s/ Donald E. Brandt
Donald E. Brandt

Signing this letter indicates your acceptance of the terms of this offer.

Acceptance: /s/ David P. Falck Date: May 28, 2009

Attachment A

- A starting annual base salary of $450,000.
- Initial hiring incentive of $200,000 payable during the first two weeks of your employment. Second year hiring incentive of $150,000 payable within two weeks of your 1 year anniversary date (the “Second Year Incentive”). [If, within two years following the payment to you of the Second Year Incentive, you resign for any reason or your employment is terminated by the Company for Cause (as defined below), you shall immediately repay to the Company the full amount of such Incentive.]
- 5 weeks vacation annually
- Vehicle allowance of $10,000 per year
- Eligibility to participate in the officer annual incentive plan with a target payment for 2009 of 50% and up to a maximum of 100% of annual base salary. Annual incentive payments are dependent on company and business unit performance and are generally paid during the first quarter of the subsequent year. Incentive for 2009 will be prorated based on employment date.
- Long-Term Stock Based Compensation: The Human Resources Committee has approved a Long-Term award to be granted to you effective upon your hire date.

    (1) An award of 21,580 performance shares

        - 8,580 shares will vest in 2011
        - 13,000 shares will vest in 2012

    (2) An award of 22,750 restricted stock units

        - 6,500 units will vest through 2/1/2010
        - 6,500 units will vest through 2/1/2011
        - 6,500 units will vest through 2/1/2012
        - 3,250 units will vest through 2/1/2013

The awards will vest subject to your continued employment through the applicable vesting date and in all events will be subject to the terms and conditions of the plan and the applicable award agreement.

- Eligibility to participate in the Supplemental Executive Benefit Retirement Plan. The SEBRP is structured as a cash balance plan to which the company contributes 28 percent of your base and annual incentive compensation.

- Eligibility to participate in the company's 401(k) plan. You are eligible to contribute between 1 percent and 50 percent of your eligible base compensation. After six months of employment, you will become eligible for the company matching contribution of 75 cents for every dollar you contribute, up to 6 percent of your compensation.

- Eligibility to participate in the Deferred Compensation Plan (DCP.) The DCP provides you with the opportunity to defer part of your compensation on a pre-tax basis. The deferred amount also earns interest. The company sets the interest amount each calendar year.

- Special Deferred Compensation Retention Program. APS will establish a deferred compensation arrangement and provide an initial credit of $350,000. The first $250,000 credit will vest upon the fifth anniversary of your hire date and the last $100,000 credit will vest upon the seventh anniversary of your hire date, in each case, subject to your continued employment through the applicable vesting date. The initial credit will earn interest in accordance with the Pinnacle West Deferred Compensation Plan.

- You will receive a Key Executive Employment & Severance Agreements ("KEESA") that provide severance benefits in connection with a change of control on terms and conditions generally applicable to other similarly situated executives of the Company, but modified to comply with the policies set forth in the Form 8-K filed by the Company on May 4, 2009. In the event of payment under this agreement, you would receive 2.99 times base salary and annual incentive as described in the agreement.

- If you enroll in the company's benefit program within the first 30 days of employment, your medical, dental, and life insurance will be effective on your one-month anniversary date of employment. Medical and dental plan premiums are on a pre-tax basis.

- You will be eligible for the relocation benefits provided generally to the Company's senior executives.

All items of compensation, and all benefits, that are provided pursuant to a compensation or benefit plan or agreement will be subject to the terms and provisions of the relevant plan or agreement and, in all cases, the Company reserves the right to modify, amend, suspend or terminate the applicable plan or agreement.

In the event that, prior to the second anniversary of your hire date, your employment is terminated by the Company without Cause and you are not entitled to severance benefits under the KEESA, subject to your execution and non-revocation of a general release of claims against the Company and its affiliates within 55 days after your termination, you will receive continuation of your annual base salary at the rate in effect immediately preceding the date on which your employment terminates for a period of twelve months commencing on the date that is 60 days following your termination, such payments to be made in accordance with the Company's normal payroll practices as in effect on the date of termination. You will also be paid a target bonus. In addition, for a period of 12 months following your termination, you will be paid a monthly amount equal to the monthly employer-paid portion of the premiums for active senior executives' health care coverage as in effect from time to time during such 12-month period. Each payment under this paragraph will be deemed a separate payment and, to the extent required to comply with Section 409A of the Code, will be delayed until the date that is six months after your separation from service.

For purposes of this Agreement, "Cause" means (i) your engaging in conduct which has caused demonstrable and serious injury to the Company, monetary or otherwise; (ii) commission of a felony; (iii) your unreasonable neglect or refusal to perform your duties or responsibilities; (iv) an act by you of gross or willful misconduct; or (v) a material breach of the Company's policies that are applicable to you.

Your employment is "at will" which means that either you or the Company may terminate your employment at any time for any reason with or without notice.

You represent that you have full authority to execute this offer letter and that neither executing this letter or providing services to the Company or its affiliates will constitute a breach of any agreement that you may have with any other party.

This offer is contingent upon successful completion of a pre-employment medical screening and background check.

Exhibit 12.1

PINNACLE WEST CAPITAL CORPORATION
COMPUTATION OF EARNINGS TO FIXED CHARGES
(dollars in thousands)

	Three Months Ended March 31,	Twelve Months Ended December 31,				
	2010	2009	2008	2007	2006	2005
Earnings:						
Income (loss) from continuing operations attributable to common shareholders	$ (5,889)	$ 82,006	$ 231,304	$ 300,436	$ 308,972	$ 223,933
Income taxes	(15,480)	37,827	76,897	152,006	151,122	127,361
Fixed charges	63,640	250,647	234,682	228,112	217,566	206,657
Total earnings	$ 42,271	$ 370,480	$ 542,883	$ 680,554	$ 677,660	$ 557,951
Fixed Charges:						
Interest expense	$ 62,054	$ 246,606	$ 230,145	$ 223,935	$ 214,078	$ 203,748
Estimated interest portion of annual rents	1,586	4,041	4,537	4,177	3,488	2,909
Total fixed charges	$ 63,640	$ 250,647	$ 234,682	$ 228,112	$ 217,566	$ 206,657
Ratio of Earnings to Fixed Charges (rounded down)	0.66	1.47	2.31	2.98	3.11	2.69

Exhibit 12.2

ARIZONA PUBLIC SERVICE COMPANY
COMPUTATION OF EARNINGS TO FIXED CHARGES
(dollars in thousands)

	Three Months Ended March 31,	Twelve Months Ended December 31,				
	2010	2009	2008	2007	2006	2005
Earnings:						
Income from continuing operations attributable to common shareholder	$ 10,984	$ 251,225	$ 262,344	$ 283,940	$ 269,730	$ 170,479
Income taxes	(6,283)	152,574	107,261	151,157	138,927	98,010
Fixed charges	58,229	227,274	206,896	195,144	184,059	171,126
Total earnings	$ 62,930	$ 631,073	$ 576,501	$ 630,241	$ 592,716	$ 439,615
Fixed Charges:						
Interest charges	$ 55,594	$ 218,969	$ 197,964	$ 186,702	$ 176,459	$ 164,626
Amortization of debt discount	1,137	4,675	4,702	4,639	4,363	4,085
Estimated interest portion of annual rents	1,498	3,630	4,230	3,803	3,237	2,415
Total fixed charges	$ 58,229	$ 227,274	$ 206,896	$ 195,144	$ 184,059	$ 171,126
Ratio of Earnings to Fixed Charges (rounded down)	1.08	2.77	2.78	3.22	3.22	2.56

Exhibit 12.3

PINNACLE WEST CAPITAL CORPORATION
COMPUTATION OF EARNINGS TO FIXED CHARGES
(dollars in thousands)

	Three Months Ended March 31,	Twelve Months Ended December 31,				
	2010	2009	2008	2007	2006	2005
Earnings:						
Income (loss) from continuing operations attributable to common shareholders	$ (5,889)	$ 82,006	$ 231,304	$ 300,436	$ 308,972	$ 223,933
Income taxes	(15,480)	37,827	76,897	152,006	151,122	127,361
Fixed charges	63,640	250,647	234,682	228,112	217,566	206,657
Total earnings	$ 42,271	$ 370,480	$ 542,883	$ 680,554	$ 677,660	$ 557,951
Fixed Charges:						
Interest expense	$ 62,054	$ 246,606	$ 230,145	$ 223,935	$ 214,078	$ 203,748
Estimated interest portion of annual rents	1,586	4,041	4,537	4,177	3,488	2,909
Total fixed charges	$ 63,640	$ 250,647	$ 234,682	$ 228,112	$ 217,566	$ 206,657
Preferred Stock Dividend Requirements:						
Income (loss) before income taxes	$ (21,369)	$ 119,833	$ 308,201	$ 452,442	$ 460,094	$ 351,294
Net income (loss) from continuing operations	(5,889)	82,006	231,304	300,436	308,972	223,933
Ratio of income before income taxes to net income	3.63	1.46	1.33	1.51	1.49	1.57
Preferred stock dividends	—	—	—	—	—	—
Preferred stock dividend requirements — ratio (above) times preferred stock dividends	$ —	$ —	$ —	$ —	$ —	$ —
Fixed Charges and Preferred Stock Dividend Requirements:						
Fixed charges	$ 63,640	$ 250,647	$ 234,682	$ 228,112	$ 217,566	$ 206,657
Preferred stock dividend requirements	—	—	—	—	—	—
Total	$ 63,640	$ 250,647	$ 234,682	$ 228,112	$ 217,566	$ 206,657
Ratio of Earnings to Fixed Charges (rounded down)	0.66	1.47	2.31	2.98	3.11	2.69

Exhibit 31.1

CERTIFICATION

I, Donald E. Brandt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2010.

/s/ Donald E. Brandt
Donald E. Brandt
Chairman, President and
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, James R. Hatfield, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2010.

/s/ James R. Hatfield
James R. Hatfield
Senior Vice President &
Chief Financial Officer

Exhibit 31.3

CERTIFICATION

I, Donald E. Brandt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Arizona Public Service Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2010.

/s/ Donald E. Brandt
Donald E. Brandt
Chairman and Chief Executive Officer

Exhibit 31.4

CERTIFICATION

I, James R. Hatfield, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Arizona Public Service Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2010.

/s/ James R. Hatfield
James R. Hatfield
Senior Vice President &
Chief Financial Officer

Exhibit 32.1

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

I, Donald E. Brandt, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation for the fiscal quarter ended March 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Pinnacle West Capital Corporation.

Date: May 6, 2010.

/s/ Donald E. Brandt
Donald E. Brandt
Chairman, President and
Chief Executive Officer

I, James R. Hatfield, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation for the fiscal quarter ended March 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Pinnacle West Capital Corporation.

Date: May 6, 2010.

/s/ James R. Hatfield
James R. Hatfield
Senior Vice President and
Chief Financial Officer

Exhibit 32.2

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

I, Donald E. Brandt, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Arizona Public Service Company for the fiscal quarter ended March 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Arizona Public Service Company.

Date: May 6, 2010.

/s/ Donald E. Brandt
Donald E. Brandt
Chairman and Chief Executive Officer

I, James R. Hatfield, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Arizona Public Service Company for the fiscal quarter ended March 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Arizona Public Service Company.

Date: May 6, 2010.

/s/ James R. Hatfield
James R. Hatfield
Senior Vice President and
Chief Financial Officer