

STRATEGIC HOTELS & RESORTS, INC
Form 8-K
March 16, 2006

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 8-K

Current Report

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): **March 11, 2006**

Strategic Hotels & Resorts, Inc.

(Exact Name of Registrant as specified in its charter)

Maryland (State or other jurisdiction of incorporation)	001-32223 (Commission File Number)	33-1082757 (IRS Employer Identification No.)
<u>77 West Wacker Drive, Suite 4600, Chicago, Illinois 60601</u>		

(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: **(312) 658-5000**

Strategic Hotel Capital, Inc.

(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 5.02 Departure of Directors or Principal Officers; Election of Directors; Appointment of Principal Officers

(b) On March 11, 2006, each of Mr. Thomas A. Hassard and Mr. Robert J. Watson notified Strategic Hotels & Resorts, Inc. (the Company) that they will resign from their position as directors of the Company effective March 13, 2006.

(d) Effective March 15, 2006, the board of directors (the Board) of the Company unanimously approved the appointment of Edward C. Coppola, David Michael Charles Michels and William A. Prezant as directors of the Company. Messrs. Coppola, Michels and Prezant will serve until the 2006 annual meeting of shareholders, or until such time as their successors are duly elected and qualified. The Board determined that Messrs. Coppola, Michels and Prezant are independent under the listing standards of the New York Stock Exchange.

A copy of the Company's press release announcing the foregoing is attached hereto as Exhibit 99.1 and is incorporated herein by reference.

Item 9.01 Financial Statements and Exhibits.

(c) Exhibits.

99.1 Press Release dated March 14, 2006.

SIGNATURES

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

STRATEGIC HOTELS & RESORTS, INC.

By: /s/ Monte J. Huber
Name: Monte J. Huber
Title: Vice President, Controller and Treasurer

Date: March 16, 2006

Exhibit Index

99.1 Press Release dated March 14, 2006.

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Decrease 1%

—

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(a) Each fluctuation assumes that the other assumptions of the calculation are held constant while the rates are changed by one percentage point.

The following chart reflects the sensitivities that a change in certain actuarial assumptions would have had on the December 31, 2018 other postretirement benefit obligation and our 2018 reported other postretirement benefit expense, after consideration of amounts capitalized or billed to electric plant participants, on Pinnacle West's Consolidated Statements of Income (dollars in millions):

Increase (Decrease)

Actuarial Assumption (a)	Impact on Postretirement Benefit Obligation	Other Impact on Postretirement Benefit Expense
Discount rate:		
Increase 1%	\$ (85)	\$ (1)
Decrease 1%	108	6
Healthcare cost trend rate (b):		
Increase 1%	101	10
Decrease 1%	(81)	(4)
Expected long-term rate of return on plan assets – pretax:		
Increase 1%	—	(5)
Decrease 1%	—	5

(a) Each fluctuation assumes that the other assumptions of the calculation are held constant while the rates are changed by one percentage point.

(b) This assumes a 1% change in the initial and ultimate healthcare cost trend rate.

See Notes 2 and 7 for further details about our pension and other postretirement benefit plans.

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Fair Value Measurements

We account for derivative instruments, investments held in our nuclear decommissioning trust fund, investments held in our other special use funds, certain cash equivalents, and plan assets held in our retirement and other benefit plans at fair value on a recurring basis. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We use inputs, or assumptions that market participants would use, to determine fair market value. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The significance of a particular input determines how the instrument is classified in a fair value hierarchy. The determination of fair value sometimes requires subjective and complex judgment. Our assessment of the inputs and the significance of a particular input to fair value measurement may affect the valuation of the instruments and their placement within a fair value hierarchy. Actual results could differ from our estimates of fair value. See Note 1 for a discussion of accounting policies and Note 13 for fair value measurement disclosures.

Asset Retirement Obligations

We recognize an ARO for the future decommissioning or retirement of our tangible long-lived assets for which a legal obligation exists. The ARO liability represents an estimate of the fair value of the current obligation related to decommissioning and the retirement of those assets. ARO measurements inherently involve uncertainty in the amount and timing of settlement of the liability. We use an expected cash flow approach to measure the amount we recognize as an ARO. This approach applies probability weighting to discounted future cash flow scenarios that reflect a range of possible outcomes. The scenarios consider settlement of the ARO at the expiration of the asset's current license or lease term and expected decommissioning dates. The fair value of an ARO is recognized in the period in which it is incurred. The associated asset retirement costs are capitalized as part of the carrying value of the long-lived asset and are depreciated over the life of the related assets. In addition, we accrete the ARO liability to reflect the passage of time. Changes in these estimates and assumptions could materially affect the amount of the recorded ARO for these assets. In accordance with GAAP accounting, APS accrues removal costs for its regulated utility assets, even if there is no legal obligation for removal.

AROs as of December 31, 2018 are described further in Note 11.

Income Taxes

Our income tax expense, deferred tax assets and liabilities, and liabilities for unrecognized tax benefits reflect management's best estimate of current and future taxes to be paid. On December 22, 2017, the Tax Act was enacted, and is generally effective January 1, 2018. This legislation made significant changes to the federal income tax laws. Changes which impact the Company include, but are not limited to, a reduction in the corporate tax rate to 21%, revisions to the rules related to tax bonus depreciation, limitations on interest deductibility and an associated exception for certain public utility property, and requirements that certain excess deferred tax amounts of regulated utilities be normalized. Deferred tax assets or liabilities are recognized for the estimated future tax effects attributable to temporary differences between the financial statement basis and the tax basis of assets and liabilities as well as tax credit carryforwards and net operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period the change is enacted. Given the regulatory nature of the Company's business, substantially all of the effect on deferred tax assets and liabilities for the reduction in the federal corporate tax

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rate to 21% was recorded as a regulatory liability recoverable by ratepayers as of December 31, 2017. See Note 3 for further discussion of the accounting for the regulatory liability. The calculation of our tax liabilities involves dealing with the application of complex laws and regulations which are voluminous and often ambiguous. Interpretations and guidance surrounding income tax laws and regulations change over time. Tax positions taken by Pinnacle West on its income tax returns that are recognized in the financial statements must satisfy a "more likely than not" recognition threshold, assuming that the position will be sustained upon examination by taxing authorities with full knowledge of all relevant information, including resolutions of any related appeals or litigation processes, on the basis of the technical merits. Additional guidance may be issued through legislation, Treasury regulations, or other technical guidance, which may materially affect amounts the Company has recognized in its financial statements.

We record unrecognized tax benefits for tax positions that may not satisfy this "more likely than not" recognition threshold as liabilities in accordance with generally accepted accounting principles. These liabilities are adjusted when management judgment changes as a result of the evaluation of new information not previously available. These changes will be reflected as an increase or decrease to income tax expense in the period in which new information is available.

OTHER ACCOUNTING MATTERS

We adopted the following new accounting standards on January 1, 2018:

• ASU 2014-09: Revenue from Contracts with Customers, and related amendments

• ASU 2016-01: Financial Instruments, Recognition and Measurement

• ASU 2016-15: Statement of Cash Flows, Classification of Certain Cash Receipts and Cash Payments

• ASU 2016-18: Statement of Cash Flows, Restricted Cash

• ASU 2017-01: Business Combinations, Clarifying the Definition of a Business

• ASU 2017-05: Other Income, Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets

• ASU 2017-07: Compensation-Retirement Benefits, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

• ASU 2018-02: Income Statement-Reporting Comprehensive Income, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

We adopted the following new accounting standards on January 1, 2019:

• ASU 2016-02: Leases, and related amendments

• ASU 2017-12: Derivatives and Hedging, Targeted Improvements to Accounting for Hedging Activities

We are currently evaluating the impacts of the pending adoption of the following new accounting standards effective for us on January 1, 2020:

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- ASU 2016-13: Financial Instruments, Measurement of Credit Losses

- ASU 2018-15: Internal-Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract

See Note 2 for additional information related to new accounting standards.

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 and benefit plan assets.

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, other special use funds (see Note 13 and Note 19), and benefit plan assets. The nuclear decommissioning trust, other special use funds and benefit plan assets also have risks associated with the changing market value of their equity and other non-fixed income investments. Nuclear decommissioning and benefit plan costs are recovered in regulated electricity prices.

The tables below present contractual balances of our consolidated long-term and short-term debt at the expected maturity dates, as well as the fair value of those instruments on December 31, 2018 and 2017. The interest rates presented in the tables below represent the weighted-average interest rates as of December 31, 2018 and 2017 (dollars in millions):

Pinnacle West – Consolidated

	Short-Term Debt Interest Rates		Variable-Rate Long-Term Debt Interest Rates		Fixed-Rate Long-Term Debt Interest Rates	
	Rates	Amount	Rates	Amount	Rates	Amount
2018						
2019	2.99%	\$ 76	—	—	8.75%	\$500
2020	—	—	3.02 %	150	2.23 %	550

2021	—	—	—	—	—	—
2022	—	—	—	—	—	—
2023	—	—	—	—	—	—
Years thereafter	—	—	1.76 %	36	4.25 %	3,940
Total		\$ 76		\$ 186		\$4,990
Fair value		\$ 76		\$ 186		\$5,048

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	Short-Term Debt Interest		Variable-Rate Long-Term Debt Interest		Fixed-Rate Long-Term Debt Interest	
	Rates	Amount	Rates	Amount	Rates	Amount
2017						
2018	2.14%	\$ 95	2.17 %	\$ 50	1.75%	\$32
2019	—	—	2.27 %	100	8.75%	500
2020	—	—	—	—	2.23%	550
2021	—	—	—	—	—	—
2022	—	—	—	—	—	—
Years thereafter	—	—	1.77 %	36	4.25%	3,640
Total		\$ 95		\$ 186		\$4,722
Fair value		\$ 95		\$ 186		\$5,119

The tables below present contractual balances of APS's long-term and short-term debt at the expected maturity dates, as well as the fair value of those instruments on December 31, 2018 and 2017. The interest rates presented in the tables below represent the weighted-average interest rates as of December 31, 2018 and 2017 (dollars in millions):

APS — Consolidated

	Variable-Rate Long-Term Debt Interest		Fixed-Rate Long-Term Debt Interest	
	Rates	Amount	Rates	Amount
2018				
2019	—	—	8.75 %	\$500
2020	—	—	2.20%	250
2021	—	—	—	—
2022	—	—	—	—
2023	—	—	—	—
Years thereafter	1.76 %	36	4.25 %	3,940
Total		\$ 36		\$4,690
Fair value		\$ 36		\$4,754

	Variable-Rate Long-Term Debt Interest		Fixed-Rate Long-Term Debt Interest	
	Rates	Amount	Rates	Amount
2017				
2018	2.17 %	\$ 50	1.75%	\$32
2019	2.27 %	100	8.75%	500
2020	—	—	2.20%	250
2021	—	—	—	—
2022	—	—	—	—

Years thereafter	1.77 %	36	4.25 %	3,640
Total		\$ 186		\$4,422
Fair value		\$ 186		\$4,820

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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 may qualify as derivatives, including futures, 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 in 2018 and 2017 (dollars in millions):

	2018	2017
Mark-to-market of net positions at beginning of year	\$(91)	\$(49)
Decrease (Increase) in regulatory asset	31	(46)
Recognized in OCI:		
Mark-to-market losses realized during the period	2	4
Change in valuation techniques	—	—
Mark-to-market of net positions at end of year	\$(58)	\$(91)

The table below shows the fair value of maturities of our derivative contracts (dollars in millions) at December 31, 2018 by maturities and by the type of valuation that is performed to calculate the fair values, classified in their entirety based on the lowest level of input that is significant to the fair value measurement. See Note 1, “Derivative Accounting” and “Fair Value Measurements,” for more discussion of our valuation methods.

Source of Fair Value	2019	2020	2021	2022	2023	Total fair value
Observable prices provided by other external sources	\$(29)	\$(10)	\$(7)	\$(4)	\$	—\$(50)
Prices based on unobservable inputs	(4)	(4)	—	—	—	(8)
Total by maturity	\$(33)	\$(14)	\$(7)	\$(4)	\$	—\$(58)

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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 Consolidated Balance Sheets at December 31, 2018 and 2017 (dollars in millions):

	December 31, 2018		December 31, 2017	
	Gain (Loss)		Gain (Loss)	
	Price Up 10%	Price Down 10%	Price Up 10%	Price Down 10%
Mark-to-market changes reported in:				
Regulatory asset (liability) (a)				
Electricity	\$ 1	\$ (1)	\$ 1	\$ (1)
Natural gas	44	(44)	45	(45)
Total	\$ 45	\$ (45)	\$ 46	\$ (46)

These contracts are economic hedges of our forecasted purchases of natural gas and electricity. The impact of these hypothetical price movements would substantially offset (a) 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 16 for a discussion of our credit valuation adjustment policy.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See "Market and Credit Risks" in Item 7 above for a discussion of quantitative and qualitative disclosures about market risks.

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FINANCIAL STATEMENT SCHEDULES

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See Note 12 for the selected quarterly financial data (unaudited) required to be presented in this Item.

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**MANAGEMENT’S REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
(PINNACLE WEST CAPITAL CORPORATION)**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f), for Pinnacle West. Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control — Integrated Framework (2013)*, our management concluded that our internal control over financial reporting was effective as of December 31, 2018. The effectiveness of our internal control over financial reporting as of December 31, 2018 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which is included herein and also relates to the Company’s consolidated financial statements.

February 22, 2019

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors of
Pinnacle West Capital Corporation
Phoenix, Arizona

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Pinnacle West Capital Corporation and subsidiaries (the "Company") as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in equity, and cash flows, for each of the three years in the period ended December 31, 2018, the related notes and the schedules listed in the Index at Item 15 (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by COSO.

Basis for Opinions

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards

require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures to respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte & Touche LLP

Phoenix, Arizona
February 22, 2019

We have served as the Company's auditor since 1932.

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

	Year Ended December 31,		
	2018	2017	2016
OPERATING REVENUES (NOTE 20)	\$3,691,247	\$3,565,296	\$3,498,682
OPERATING EXPENSES			
Fuel and purchased power	1,076,116	981,301	1,075,510
Operations and maintenance	1,036,744	949,107	931,692
Depreciation and amortization	582,354	534,118	485,829
Taxes other than income taxes	212,849	184,347	166,499
Other expenses	9,497	6,660	3,541
Total	2,917,560	2,655,533	2,663,071
OPERATING INCOME	773,687	909,763	835,611
OTHER INCOME (DEDUCTIONS)			
Allowance for equity funds used during construction (Note 1)	52,319	47,011	42,140
Pension and other postretirement non-service credits - net (Note 7)	49,791	24,664	20,373
Other income (Note 17)	24,896	4,006	901
Other expense (Note 17)	(17,966)	(21,539)	(15,337)
Total	109,040	54,142	48,077
INTEREST EXPENSE			
Interest charges	243,465	219,796	205,720
Allowance for borrowed funds used during construction (Note 1)	(25,180)	(22,112)	(19,970)
Total	218,285	197,684	185,750
INCOME BEFORE INCOME TAXES	664,442	766,221	697,938
INCOME TAXES (Note 4)	133,902	258,272	236,411
NET INCOME	530,540	507,949	461,527
Less: Net income attributable to noncontrolling interests (Note 18)	19,493	19,493	19,493
NET INCOME ATTRIBUTABLE TO COMMON SHAREHOLDERS	\$511,047	\$488,456	\$442,034
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — BASIC	112,129	111,839	111,409
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — DILUTED	112,550	112,367	112,046
EARNINGS PER WEIGHTED-AVERAGE COMMON SHARE OUTSTANDING			
Net income attributable to common shareholders — basic	\$4.56	\$4.37	\$3.97
Net income attributable to common shareholders — diluted	\$4.54	\$4.35	\$3.95

The accompanying notes are an integral part of the financial statements.

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PINNACLE WEST CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(dollars in thousands)

	Year Ended December 31,		
	2018	2017	2016
NET INCOME	\$530,540	\$507,949	\$461,527
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX			
Derivative instruments:			
Net unrealized loss, net of tax benefit (expense) of (\$78), \$24, and (\$585) (Note 16)	(78	) (35	) (538
Reclassification of net realized loss, net of tax benefit of \$473, \$1,294, and \$985 (Note 16)	1,527	2,225	2,941
Pension and other postretirement benefits activity, net of tax benefit (expense) of (\$1,585), \$693, and \$633 (Note 7)	4,397	(3,370	) (1,477
Total other comprehensive income (loss)	5,846	(1,180	) 926
COMPREHENSIVE INCOME	536,386	506,769	462,453
Less: Comprehensive income attributable to noncontrolling interests	19,493	19,493	19,493
COMPREHENSIVE INCOME ATTRIBUTABLE TO COMMON SHAREHOLDERS	\$516,893	\$487,276	\$442,960

The accompanying notes are an integral part of the financial statements.

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

	December 31, 2018	2017
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$5,766	\$13,892
Customer and other receivables	267,887	305,147
Accrued unbilled revenues	137,170	112,434
Allowance for doubtful accounts	(4,069)	(2,513)
Materials and supplies (at average cost)	269,065	264,012
Fossil fuel (at average cost)	25,029	25,258
Assets from risk management activities (Note 16)	1,113	1,931
Deferred fuel and purchased power regulatory asset (Note 3)	37,164	75,637
Other regulatory assets (Note 3)	129,738	172,451
Other current assets	56,128	48,039
Total current assets	924,991	1,016,288
INVESTMENTS AND OTHER ASSETS		
Nuclear decommissioning trust (Notes 13 and 19)	851,134	871,000
Other special use funds (Notes 13 and 19)	236,101	32,542
Other assets	103,247	52,040
Total investments and other assets	1,190,482	955,582
PROPERTY, PLANT AND EQUIPMENT (Notes 1, 6 and 9)		
Plant in service and held for future use	18,736,628	17,798,061
Accumulated depreciation and amortization	(6,366,014)	(6,128,535)
Net	12,370,614	11,669,526
Construction work in progress	1,170,062	1,291,498
Palo Verde sale leaseback, net of accumulated depreciation of \$245,275 and \$241,405 (Note 18)	105,775	109,645
Intangible assets, net of accumulated amortization of \$591,202 and \$582,272	262,902	257,189
Nuclear fuel, net of accumulated amortization of \$137,850 and \$144,070	120,217	117,408
Total property, plant and equipment	14,029,570	13,445,266
DEFERRED DEBITS		
Regulatory assets (Notes 1, 3 and 4)	1,342,941	1,202,302
Assets for other postretirement benefits (Note 7)	46,906	268,978
Other	129,312	130,666
Total deferred debits	1,519,159	1,601,946
TOTAL ASSETS	\$17,664,202	\$17,019,082

The accompanying notes are an integral part of the financial statements.

Table of Contents**PINNACLE WEST CAPITAL CORPORATION
CONSOLIDATED BALANCE SHEETS**

(dollars in thousands)

	December 31,	
	2018	2017
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$277,336	\$256,442
Accrued taxes	154,819	148,946
Accrued interest	61,107	56,397
Common dividends payable	82,675	77,667
Short-term borrowings (Note 5)	76,400	95,400
Current maturities of long-term debt (Note 6)	500,000	82,000
Customer deposits	91,174	70,388
Liabilities from risk management activities (Note 16)	35,506	59,252
Liabilities for asset retirements (Note 11)	19,842	4,745
Regulatory liabilities (Note 3)	165,876	100,086
Other current liabilities	184,229	246,529
Total current liabilities	1,648,964	1,197,852
LONG-TERM DEBT LESS CURRENT MATURITIES (Note 6)	4,638,232	4,789,713
DEFERRED CREDITS AND OTHER		
Deferred income taxes (Note 4)	1,807,421	1,690,805
Regulatory liabilities (Notes 1, 3, 4 and 7)	2,325,976	2,452,536
Liabilities for asset retirements (Note 11)	706,703	674,784
Liabilities for pension benefits (Note 7)	443,170	327,300
Liabilities from risk management activities (Note 16)	24,531	37,170
Customer advances	137,153	113,996
Coal mine reclamation	212,785	231,597
Deferred investment tax credit	200,405	205,575
Unrecognized tax benefits (Note 4)	22,517	13,115
Other	147,640	148,909
Total deferred credits and other	6,028,301	5,895,787
COMMITMENTS AND CONTINGENCIES (SEE NOTES)		
EQUITY		
Common stock, no par value; authorized 150,000,000 shares, 112,159,896 and 111,816,170 issued at respective dates	2,634,265	2,614,805
Treasury stock at cost; 58,135 shares at end of 2018 and 64,463 shares at end of 2017	(4,825	) (5,624
Total common stock	2,629,440	2,609,181
Retained earnings	2,641,183	2,442,511
Accumulated other comprehensive loss (Note 21)	(47,708	) (45,002
Total shareholders' equity	5,222,915	5,006,690
Noncontrolling interests (Note 18)	125,790	129,040
Total equity	5,348,705	5,135,730
TOTAL LIABILITIES AND EQUITY	\$ 17,664,202	\$ 17,019,082

The accompanying notes are an integral part of the financial statements.

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

	Year Ended December 31,		
	2018	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Net Income	\$530,540	\$507,949	\$461,527
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization including nuclear fuel	650,955	610,629	565,011
Deferred fuel and purchased power	(78,277)	(48,405)	(60,303)
Deferred fuel and purchased power amortization	116,750	(14,767)	38,152
Allowance for equity funds used during construction	(52,319)	(47,011)	(42,140)
Deferred income taxes	117,355	248,164	206,870
Deferred investment tax credit	(5,170)	(4,587)	23,082
Change in derivative instruments fair value	—	(373)	(403)
Stock compensation	19,547	20,502	18,883
Changes in current assets and liabilities:			
Customer and other receivables	37,530	(93,797)	(2,489)
Accrued unbilled revenues	(24,736)	(4,485)	(11,709)
Materials, supplies and fossil fuel	(6,103)	(6,683)	(1,491)
Income tax receivable	—	3,751	(3,162)
Other current assets	33,844	(10,580)	(23,324)
Accounts payable	(14,602)	(23,769)	(66,917)
Accrued taxes	6,597	9,982	447
Other current liabilities	28,174	19,154	29,594
Change in margin and collateral accounts — assets	143	(300)	673
Change in margin and collateral accounts — liabilities	(2,211)	(533)	17,735
Change in unrecognized tax benefits	(1,235)	5,891	1,628
Change in long-term regulatory liabilities	(109,284)	45,764	14,682
Change in other long-term assets	78,604	(68,480)	(60,163)
Change in other long-term liabilities	(48,958)	(29,980)	(82,793)
Net cash flow provided by operating activities	1,277,144	1,118,036	1,023,390
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures	(1,178,169)	(1,408,774)	(1,275,472)
Contributions in aid of construction	27,716	23,708	64,296
Allowance for borrowed funds used during construction	(25,180)	(22,112)	(19,970)
Proceeds from nuclear decommissioning trust sales and other special use funds	653,033	542,246	633,410
Investment in nuclear decommissioning trust and other special use funds	(672,165)	(544,527)	(635,691)
Other	1,941	(19,078)	(18,651)
Net cash flow used for investing activities	(1,192,824)	(1,428,537)	(1,252,078)
CASH FLOWS FROM FINANCING ACTIVITIES			
Issuance of long-term debt	445,245	848,239	693,151
Repayment of long-term debt	(182,000)	(125,000)	(370,430)
Short-term borrowings and (repayments) — net	(7,000)	(107,800)	137,200
Short-term debt borrowings under revolving credit facility	45,000	58,000	40,000
Short-term debt repayments under revolving credit facility	(57,000)	(32,000)	—
Dividends paid on common stock	(308,892)	(289,793)	(274,229)

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Common stock equity issuance and purchases - net	(5,055)	(13,390)	(4,867)
Distributions to noncontrolling interests	(22,744)	(22,744)	(22,744)
Net cash flow (used for) provided by financing activities	(92,446)	315,512	198,081
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(8,126)	5,011	(30,607)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	13,892	8,881	39,488
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$5,766	\$13,892	\$8,881

The accompanying notes are an integral part of the financial statements.

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PINNACLE WEST CAPITAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(dollars in thousands, except per share amounts)

	Common Stock		Treasury Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total
	Shares	Amount	Shares	Amount				
Balance, December 31, 2015	111,095,402	\$2,541,668	(115,030)	\$(5,806)	\$2,092,803	\$ (44,748)	\$ 135,540	\$4,719,457
Net income	—	—	—	—	442,034	—	19,493	461,527
Other comprehensive income	—	—	—	—	—	926	—	926
Dividends on common stock (\$2.56 per share)	—	—	—	—	(284,765)	—	—	(284,765)
Issuance of common stock	296,651	13,982	—	—	—	—	—	13,982
Purchase of treasury stock (a)	—	—	(128,105)	(9,087)	—	—	—	(9,087)
Reissuance of treasury stock for stock-based compensation and other	—	—	187,818	10,760	—	—	—	10,760
Stock compensation cumulative effect adjustments (b)	—	40,380	—	—	5,475	—	—	45,855
Net capital activities by noncontrolling interests	—	—	—	—	—	—	(22,743)	(22,743)
Balance, December 31, 2016	111,392,053	2,596,030	(55,317)	(4,133)	2,255,547	(43,822)	132,290	4,935,912
Net income	—	—	—	—	488,456	—	19,493	507,949
Other comprehensive loss	—	—	—	—	—	(1,180)	—	(1,180)
Dividends on common stock (\$2.70 per share)	—	—	—	—	(301,492)	—	—	(301,492)
Issuance of common stock	424,117	18,775	—	—	—	—	—	18,775
Purchase of treasury stock (a)	—	—	(216,911)	(17,755)	—	—	—	(17,755)
Reissuance of treasury stock for stock-based compensation and other	—	—	207,765	16,264	—	—	—	16,264
Net capital activities by noncontrolling interests	—	—	—	—	—	—	(22,743)	(22,743)
Balance, December 31, 2017	111,816,170	2,614,805	(64,463)	(5,624)	2,442,511	(45,002)	129,040	5,135,730
Net income	—	—	—	—	511,047	—	19,493	530,540
Other comprehensive income	—	—	—	—	—	5,846	—	5,846
Dividends on common stock (\$2.87 per share)	—	—	—	—	(320,927)	—	—	(320,927)
Issuance of common stock	343,726	19,460	—	—	—	—	—	19,460
Purchase of treasury stock (a)	—	—	(129,903)	(10,338)	—	—	—	(10,338)
Reissuance of treasury stock for stock-based compensation and other	—	—	136,231	11,137	—	—	—	11,137
Net capital activities by noncontrolling interests	—	—	—	—	—	—	(22,743)	(22,743)
Reclassification of income tax effects related to new tax reform (See Note 2)	—	—	—	—	8,552	(8,552)	—	—
Balance, December 31, 2018	112,159,896	\$2,634,265	(58,135)	\$(4,825)	\$2,641,183	\$ (47,708)	\$ 125,790	\$5,348,705

(a) Primarily represents shares of common stock withheld from certain stock awards for tax purposes.

(b) During 2016, we adopted new stock-based compensation accounting guidance.

The accompanying notes are an integral part of the financial statements.

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**MANAGEMENT’S REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
(ARIZONA PUBLIC SERVICE COMPANY)**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f), for APS. Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control — Integrated Framework (2013)*, our management concluded that our internal control over financial reporting was effective as of December 31, 2018. The effectiveness of our internal control over financial reporting as of December 31, 2018 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which is included herein and also relates to the Company’s financial statements.

February 22, 2019

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors of
Arizona Public Service Company
Phoenix, Arizona

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Arizona Public Service Company and subsidiaries (the "Company") as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in equity, and cash flows, for each of the three years in the period ended December 31, 2018, and the related notes and the schedule listed in the Index at Item 15 (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by COSO.

Basis for Opinions

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards

require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures to respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte & Touche LLP

Phoenix, Arizona
February 22, 2019

We have served as the Company's auditor since 1932.

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

	Year Ended December 31,		
	2018	2017	2016
OPERATING REVENUES	\$3,688,342	\$3,557,652	\$3,498,090
OPERATING EXPENSES			
Fuel and purchased power	1,094,020	992,744	1,082,625
Operations and maintenance	969,227	917,983	902,467
Depreciation and amortization	580,694	532,423	484,909
Taxes other than income taxes	212,136	183,254	166,064
Other expense	2,497	6,709	3,540
Total	2,858,574	2,633,113	2,639,605
OPERATING INCOME	829,768	924,539	858,485
OTHER INCOME (DEDUCTIONS)			
Allowance for equity funds used during construction (Note 1)	52,319	47,011	42,140
Pension and other postretirement non-service credits - net (Note 7)	51,242	24,371	20,224
Other income (Note 17)	22,746	3,013	271
Other expense (Note 17)	(15,292)	(13,913)	(10,554)
Total	111,015	60,482	52,081
INTEREST EXPENSE			
Interest charges	231,391	214,163	202,571
Allowance for borrowed funds used during construction (Note 1)	(25,180)	(22,112)	(19,481)
Total	206,211	192,051	183,090
INCOME BEFORE INCOME TAXES	734,572	792,970	727,476
INCOME TAXES (Note 4)	144,814	269,168	245,842
NET INCOME	589,758	523,802	481,634
Less: Net income attributable to noncontrolling interests (Note 18)	19,493	19,493	19,493
NET INCOME ATTRIBUTABLE TO COMMON SHAREHOLDER	\$570,265	\$504,309	\$462,141

The accompanying notes are an integral part of the financial statements.

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

	Year Ended December 31,		
	2018	2017	2016
NET INCOME	\$589,758	\$523,802	\$481,634
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX			
Derivative instruments:			
Net unrealized loss, net of tax benefit (expense) of (\$78), \$24, and (\$585) (Note 16)	(78	) (35	) (538
Reclassification of net realized loss, net of tax benefit of \$473, \$1,294, and \$985 (Note 16)	1,527	2,225	2,941
Pension and other postretirement benefits activity, net of tax benefit (expense) of (\$1,159), \$977, and \$293 (Note 7)	3,465	(3,750	) (729
Total other comprehensive income (loss)	4,914	(1,560	) 1,674
COMPREHENSIVE INCOME	594,672	522,242	483,308
Less: Comprehensive income attributable to noncontrolling interests	19,493	19,493	19,493
COMPREHENSIVE INCOME ATTRIBUTABLE TO COMMON SHAREHOLDER	\$575,179	\$502,749	\$463,815

The accompanying notes are an integral part of the financial statements.

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

	December 31, 2018	2017
ASSETS		
PROPERTY, PLANT AND EQUIPMENT (Notes 1, 6 and 9)		
Plant in service and held for future use	\$ 18,733,142	\$ 17,654,078
Accumulated depreciation and amortization	(6,362,771)	(6,041,965)
Net	12,370,371	11,612,113
Construction work in progress	1,170,062	1,266,636
Palo Verde sale leaseback, net of accumulated depreciation of \$245,275 and \$241,405 (Note 18)	105,775	109,645
Intangible assets, net of accumulated amortization of \$590,069 and \$581,135	262,746	257,028
Nuclear fuel, net of accumulated amortization of \$137,850 and \$144,070	120,217	117,408
Total property, plant and equipment	14,029,171	13,362,830
INVESTMENTS AND OTHER ASSETS		
Nuclear decommissioning trust (Notes 13 and 19)	851,134	871,000
Other special use funds (Notes 13 and 19)	236,101	30,358
Other assets	40,817	36,796
Total investments and other assets	1,128,052	938,154
CURRENT ASSETS		
Cash and cash equivalents	5,707	13,851
Customer and other receivables	257,654	292,791
Accrued unbilled revenues	137,170	112,434
Allowance for doubtful accounts	(4,069)	(2,513)
Materials and supplies (at average cost)	269,065	262,630
Fossil fuel (at average cost)	25,029	25,258
Assets from risk management activities (Note 16)	1,113	1,931
Deferred fuel and purchased power regulatory asset (Note 3)	37,164	75,637
Other regulatory assets (Note 3)	129,738	172,451
Other current assets	35,111	41,055
Total current assets	893,682	995,525
DEFERRED DEBITS		
Regulatory assets (Notes 1, 3, and 4)	1,342,941	1,202,302
Assets for other postretirement benefits (Note 7)	43,212	265,139
Other	128,265	129,801
Total deferred debits	1,514,418	1,597,242
TOTAL ASSETS	\$ 17,565,323	\$ 16,893,751

The accompanying notes are an integral part of the financial statements.

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

	December 31, 2018	2017
LIABILITIES AND EQUITY		
CAPITALIZATION		
Common stock	\$ 178,162	\$ 178,162
Additional paid-in capital	2,721,696	2,571,696
Retained earnings	2,788,256	2,533,954
Accumulated other comprehensive loss (Note 21)	(27,107)	(26,983)
Total shareholder equity	5,661,007	5,256,829
Noncontrolling interests (Note 18)	125,790	129,040
Total equity	5,786,797	5,385,869
Long-term debt less current maturities (Note 6)	4,189,436	4,491,292
Total capitalization	9,976,233	9,877,161
CURRENT LIABILITIES		
Current maturities of long-term debt (Note 6)	500,000	82,000
Accounts payable	266,277	247,852
Accrued taxes	176,357	157,349
Accrued interest	60,228	55,533
Common dividends payable	82,700	77,700
Customer deposits	91,174	70,388
Liabilities from risk management activities (Note 16)	35,506	59,252
Liabilities for asset retirements (Note 11)	19,842	4,192
Regulatory liabilities (Note 3)	165,876	100,086
Other current liabilities	178,137	243,922
Total current liabilities	1,576,097	1,098,274
DEFERRED CREDITS AND OTHER		
Deferred income taxes (Note 4)	1,812,664	1,742,485
Regulatory liabilities (Notes 1, 3, and 4)	2,325,976	2,452,536
Liabilities for asset retirements (Note 11)	706,703	666,527
Liabilities for pension benefits (Note 7)	425,404	306,542
Liabilities from risk management activities (Note 16)	24,531	37,170
Customer advances	137,153	113,996
Coal mine reclamation	212,785	215,830
Deferred investment tax credit	200,405	205,575
Unrecognized tax benefits (Note 4)	41,861	43,876
Other	125,511	133,779
Total deferred credits and other	6,012,993	5,918,316
COMMITMENTS AND CONTINGENCIES (SEE NOTES)		
TOTAL LIABILITIES AND EQUITY	\$ 17,565,323	\$ 16,893,751

The accompanying notes are an integral part of the financial statements.

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

	Year Ended December 31,		
	2018	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	\$ 589,758	\$ 523,802	\$ 481,634
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization including nuclear fuel	649,295	608,935	564,091
Deferred fuel and purchased power	(78,277)	(48,405)	(60,303)
Deferred fuel and purchased power amortization	116,750	(14,767)	38,152
Allowance for equity funds used during construction	(52,319)	(47,011)	(42,140)
Deferred income taxes	59,927	249,465	221,167
Deferred investment tax credit	(5,170)	(4,587)	23,082
Change in derivative instruments fair value	—	(373)	(403)
Changes in current assets and liabilities:			
Customer and other receivables	35,406	(68,040)	(1,601)
Accrued unbilled revenues	(24,736)	(4,485)	(11,709)
Materials, supplies and fossil fuel	(6,206)	(6,503)	(1,454)
Income tax receivable	—	11,174	(14,567)
Other current assets	31,707	(6,775)	(21,640)
Accounts payable	(15,608)	(26,561)	(67,543)
Accrued taxes	19,008	26,773	(13,912)
Other current liabilities	25,070	27,912	5,097
Change in margin and collateral accounts — assets	143	(300)	673
Change in margin and collateral accounts — liabilities	(2,211)	(533)	17,735
Change in unrecognized tax benefits	(1,235)	5,891	1,628
Change in long-term regulatory liabilities	(109,284)	45,764	14,682
Change in other long-term assets	77,952	(78,540)	(45,866)
Change in other long-term liabilities	(55,169)	(31,106)	(76,855)
Net cash flow provided by operating activities	1,254,801	1,161,730	1,009,948
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures	(1,169,061)	(1,381,930)	(1,248,010)
Contributions in aid of construction	27,716	23,708	64,296
Allowance for borrowed funds used during construction	(25,180)	(22,112)	(19,481)
Proceeds from nuclear decommissioning trust sales and other special use funds	653,033	542,246	633,410
Investment in nuclear decommissioning trust and other special use funds	(672,165)	(544,527)	(635,691)
Other	(1,789)	(18,538)	(13,865)
Net cash flow used for investing activities	(1,187,446)	(1,401,153)	(1,219,341)
CASH FLOWS FROM FINANCING ACTIVITIES			
Issuance of long-term debt	295,245	549,478	693,151
Repayment of long-term debt	(182,000)	—	(370,430)
Short-term borrowings and (repayments) — net	—	(135,500)	135,500
Short-term debt borrowings under revolving credit facility	25,000	—	—
Short-term debt repayments under revolving credit facility	(25,000)	—	—
Dividends paid on common stock	(316,000)	(296,800)	(281,300)
Equity infusion from Pinnacle West	150,000	150,000	42,000
Noncontrolling interests	(22,744)	(22,744)	(22,744)

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Net cash flow provided by (used for) financing activities	(75,499)	244,434	196,177
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(8,144)	5,011	(13,216)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	13,851	8,840	22,056
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$5,707	\$13,851	\$8,840
Supplemental disclosure of cash flow information:			
Cash paid (received) during the year for:			
Income taxes, net of refunds	\$77,942	\$(14,098)	\$26,864
Interest, net of amounts capitalized	196,419	184,210	181,809
Significant non-cash investing and financing activities:			
Accrued capital expenditures	\$132,620	\$130,057	\$114,874
Dividends declared but not paid	82,700	77,700	72,900

The accompanying notes are an integral part of the financial statements.

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ARIZONA PUBLIC SERVICE COMPANY
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(dollars in thousands)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total
	Shares	Amount					
Balance, December 31, 2015	71,264,947	\$ 178,162	\$ 2,379,696	\$ 2,148,493	\$ (27,097)	\$ 135,540	\$ 4,814,794
Equity infusion from Pinnacle West	—	—	42,000	—	—	—	42,000
Net income	—	—	—	462,141	—	19,493	481,634
Other comprehensive income	—	—	—	—	1,674	—	1,674
Dividends on common stock	—	—	—	(284,800)	—	—	(284,800)
Stock compensation cumulative effect adjustments (a)	—	—	—	5,411	—	—	5,411
Net capital activities by noncontrolling interests	—	—	—	—	—	(22,743)	(22,743)
Balance, December 31, 2016	71,264,947	178,162	2,421,696	2,331,245	(25,423)	132,290	5,037,970
Equity infusion from Pinnacle West	—	—	150,000	—	—	—	150,000
Net income	—	—	—	504,309	—	19,493	523,802
Other comprehensive loss	—	—	—	—	(1,560)	—	(1,560)
Dividends on common stock	—	—	—	(301,600)	—	—	(301,600)
Net capital activities by noncontrolling interests	—	—	—	—	—	(22,743)	(22,743)
Balance, December 31, 2017	71,264,947	178,162	2,571,696	2,533,954	(26,983)	129,040	5,385,869
Equity infusion from Pinnacle West	—	—	150,000	—	—	—	150,000
Net income	—	—	—	570,265	—	19,493	589,758
Other comprehensive income	—	—	—	—	4,914	—	4,914
Dividends on common stock	—	—	—	(321,001)	—	—	(321,001)
Reclassifications of income tax effects related to new tax reform (See Note 2)	—	—	—	5,038	(5,038)	—	—
Net capital activities by noncontrolling interests	—	—	—	—	—	(22,743)	(22,743)
Balance, December 31, 2018	71,264,947	\$ 178,162	\$ 2,721,696	\$ 2,788,256	\$ (27,107)	\$ 125,790	\$ 5,786,797

(a) During 2016, we adopted new stock-based compensation accounting guidance.

The accompanying notes are an integral part of the financial statements.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Description of Business and Basis of Presentation

Pinnacle West is a holding company that conducts business through its subsidiaries, APS, El Dorado, BCE and 4CA. APS, our wholly-owned subsidiary, is a vertically-integrated electric utility that provides either retail or wholesale electric service to substantially all 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 essentially all of our revenues and earnings, and is expected to continue to do so. El Dorado is an investment firm. BCE is a subsidiary that was formed in 2014 that focuses on growth opportunities that leverage the Company's core expertise in the electric energy industry. BCE is currently pursuing transmission opportunities through a joint venture arrangement. 4CA is a subsidiary that was formed in 2016 as a result of the purchase of El Paso's 7% interest in Four Corners. See Note 10 for more information on 4CA matters.

Pinnacle West's Consolidated Financial Statements include the accounts of Pinnacle West and our subsidiaries: APS, El Dorado, BCE and 4CA. APS's consolidated financial statements include the accounts of APS and certain VIEs relating to the Palo Verde sale leaseback. Intercompany accounts and transactions between the consolidated companies have been eliminated.

We consolidate VIEs for which we are the primary beneficiary. We determine whether we are the primary beneficiary of a VIE through a qualitative analysis that identifies which variable interest holder has the controlling financial interest in the VIE. In performing our primary beneficiary analysis, we consider all relevant facts and circumstances, including the design and activities of the VIE, the terms of the contracts the VIE has entered into, and which parties participated significantly in the design or redesign of the entity. We continually evaluate our primary beneficiary conclusions to determine if changes have occurred which would impact our primary beneficiary assessments. We have determined that APS is the primary beneficiary of certain VIE lessor trusts relating to the Palo Verde sale leaseback, and therefore APS consolidates these entities (see Note 18).

Our 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 consolidated financial statements and notes have been prepared consistently, with the exception of the reclassification of certain prior year amounts on our Consolidated Statements of Income and APS's Consolidated Statements of Income. Beginning in the quarter ended March 31, 2018, APS changed the format of presentation of its Consolidated Statements of Income from a utility ratemaking format to a commercial format. Minor changes were made in the description of certain income statement line items and the amounts presented in the comparable prior period also changed by immaterial amounts due to the change from a utility to a non-utility format and also from the adoption of the new accounting guidance for net periodic pension cost and net periodic postretirement benefit cost. In addition, the prior year amounts were reclassified to conform to the current year presentation for the other special use funds in the investment and other assets section on the Consolidated Balance Sheets.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Accounting Records and Use of Estimates

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.

Regulatory Accounting

APS is regulated by the ACC and FERC. The accompanying financial statements reflect the rate-making policies of these commissions. As a result, we capitalize certain costs that would be included as expense in the current period by unregulated companies. Regulatory assets represent incurred costs that have been deferred because they are probable of future recovery in customer rates. Regulatory liabilities generally represent amounts collected in rates to recover costs expected to be incurred in the future or amounts collected in excess of costs incurred and are refundable to customers.

Management continually assesses whether our regulatory assets are probable of future recovery by considering factors such as changes in the applicable regulatory environment and recent rate orders applicable to APS or other regulated entities in the same jurisdiction. This determination reflects the current political and regulatory climate in Arizona and is subject to change in the future. If future recovery of costs ceases to be probable, the assets would be written off as a charge in current period earnings.

See Note 3 for additional information.

Electric Revenues

We derive electric revenues primarily from sales of electricity to our regulated Native Load customers. Revenues related to the sale of electricity are generally recognized when service is rendered or electricity is delivered to customers. The billing of electricity sales to individual Native Load customers is based on the reading of their meters. We obtain customers' meter data on a systematic basis throughout the month, and generally bill customers within a month from when service was provided. Customers are generally

required to pay for services within 15 days of when the services are billed. Unbilled revenues are estimated by applying an average revenue/kWh by customer class to the number of estimated kWhs delivered but not billed. Differences historically between the actual and estimated unbilled revenues are immaterial. We exclude sales taxes and franchise fees on electric revenues from both revenue and taxes other than income taxes.

On January 1, 2018, we adopted new revenue guidance ASU 2014-09, Revenue from contracts with customers, accordingly our 2018 electric revenues primarily consist of activities that now are classified as revenues from contracts with customers. Our electric revenues generally represent a single performance obligation delivered over time. We have elected to apply the invoice practical expedient and, as such, we recognize revenue based on the amount to which we have a right to invoice for services performed. See Note 2.

Revenues from our Native Load customers and non-derivative instruments are reported on a gross basis on Pinnacle West's Consolidated Statements of Income. In the electricity business, some contracts to purchase electricity are netted against other contracts to sell electricity. This is called a "book-out" and usually occurs for contracts that have the same terms (quantities, delivery points and delivery periods) and for which

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power does not flow. We net these book-outs, which reduces both wholesale revenues and fuel and purchased power costs.

Some of our cost recovery mechanisms are alternative revenue programs. For alternative revenue programs that meet specified accounting criteria, we recognize revenues when the specific events permitting billing of the additional revenues have been completed.

See Notes 2 and 20 for additional information.

Allowance for Doubtful Accounts

The allowance for doubtful accounts represents our best estimate of existing accounts receivable that will ultimately be uncollectible. The allowance is calculated by applying estimated write-off factors to various classes of outstanding receivables, including accrued utility revenues. The write-off factors used to estimate uncollectible accounts are based upon consideration of both historical collections experience and management's best estimate of future collections success given the existing collections environment.

Property, Plant and Equipment

Utility plant is the term we use to describe the business property and equipment that supports electric service, consisting primarily of generation, transmission and distribution facilities. We report utility plant at its original cost, which includes:

- material and labor;
- contractor costs;
- capitalized leases;
- construction overhead costs (where applicable); and
- allowance for funds used during construction.

Pinnacle West's property, plant and equipment included in the December 31, 2018 and 2017 Consolidated Balance Sheets is composed of the following (dollars in thousands):

Property, Plant and Equipment:	2018	2017
Generation	\$8,285,514	\$7,963,998
Transmission	3,033,579	2,836,578
Distribution	6,378,345	6,025,856

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General plant	1,039,190	971,629
Plant in service and held for future use	18,736,628	17,798,061
Accumulated depreciation and amortization	(6,366,014)	(6,128,535)
Net	12,370,614	11,669,526
Construction work in progress	1,170,062	1,291,498
Palo Verde sale leaseback, net of accumulated depreciation	105,775	109,645
Intangible assets, net of accumulated amortization	262,902	257,189
Nuclear fuel, net of accumulated amortization	120,217	117,408
Total property, plant and equipment	\$14,029,570	\$13,445,266

Property, plant and equipment balances and classes for APS are not materially different than Pinnacle West.

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We expense the costs of plant outages, major maintenance and routine maintenance as incurred. We charge retired utility plant to accumulated depreciation. Liabilities associated with the retirement of tangible long-lived assets are recognized at fair value as incurred and capitalized as part of the related tangible long-lived assets. Accretion of the liability due to the passage of time is an operating expense, and the capitalized cost is depreciated over the useful life of the long-lived asset. See Note 11.

APS records a regulatory liability for the excess of the amount that has been recovered in regulated rates over the amount calculated in accordance with guidance on accounting for asset retirement obligations. APS believes it is probable it will recover in regulated rates, the costs calculated in accordance with this accounting guidance.

We record depreciation and amortization on utility plant on a straight-line basis over the remaining useful life of the related assets. The approximate remaining average useful lives of our utility property at December 31, 2018 were as follows:

- Fossil plant ~~17~~ years;
- Nuclear plant ~~23~~ years;
- Other generation ~~19~~ years;
- Transmission ~~39~~ years;
- Distribution ~~34~~ years; and
- General plant ~~6~~ years.

Depreciation of utility property, plant and equipment is computed on a straight-line, remaining-life basis. Depreciation expense was \$486 million in 2018, \$453 million in 2017, and \$422 million in 2016. For the years 2016 through 2018, the depreciation rates ranged from a low of 0.18% to a high of 19.67%. The weighted-average depreciation rate was 2.81% in 2018, 2.80% in 2017, and 2.66% in 2016.

Asset Retirement Obligations

APS has asset retirement obligations for its Palo Verde nuclear facilities and certain other generation assets. The Palo Verde asset retirement obligation primarily relates to final plant decommissioning. This obligation is based on the NRC's requirements for disposal of radiated property or plant and agreements APS reached with the ACC for final decommissioning of the plant. The non-nuclear generation asset retirement obligations

primarily relate to requirements for removing portions of those plants at the end of the plant life or lease term and coal ash pond closures. Some of APS's transmission and distribution assets have asset retirement obligations because they are subject to right of way and easement agreements that require final removal. These agreements have a history of uninterrupted renewal that APS expects to continue. As a result, APS cannot reasonably estimate the fair value of the asset retirement obligation related to such transmission and distribution assets. Additionally, APS has aquifer protection permits for some of its generation sites that require the closure of certain facilities at those sites.

See Note 11 for further information on Asset Retirement Obligations.

Allowance for Funds Used During Construction

AFUDC represents the approximate net composite interest cost of borrowed funds and an allowed return on the equity funds used for construction of regulated utility plant. Both the debt and equity components of AFUDC are non-cash amounts within the Consolidated Statements of Income. Plant

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COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

construction costs, including AFUDC, are recovered in authorized rates through depreciation when completed projects are placed into commercial operation.

AFUDC was calculated by using a composite rate of 7.03% for 2018, 6.68% for 2017, and 7.17% for 2016. APS compounds AFUDC semi-annually and ceases to accrue AFUDC when construction work is completed and the property is placed in service.

Materials and Supplies

APS values materials, supplies and fossil fuel inventory using a weighted-average cost method. APS materials, supplies and fossil fuel inventories are carried at the lower of weighted-average cost or market, unless evidence indicates that the weighted-average cost (even if in excess of market) will be recovered.

Fair Value Measurements

We apply recurring fair value measurements to cash equivalents, derivative instruments, investments held in the nuclear decommissioning trust and other special use funds. On an annual basis, we apply fair value measurements to plan assets held in our retirement and other benefits plans. Due to the short-term nature of short-term borrowings, the carrying values of these instruments approximate fair value. Fair value measurements may also be applied on a nonrecurring basis to other assets and liabilities in certain circumstances such as impairments. We also disclose fair value information for our long-term debt, which is carried at amortized cost (see Note 6).

Fair value is the price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market which we can access for the asset or liability in an orderly transaction between willing market participants on the measurement date. Inputs to fair value may include observable and unobservable data. We maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

We determine fair market value using observable inputs such as actively-quoted prices for identical instruments when available. When actively-quoted prices are not available for the identical instruments, we use other observable inputs, such as prices for similar instruments, other corroborative market information, or prices provided by other external sources. For

options, long-term contracts and other contracts for which observable price data are not available, we use models and other valuation methods, which may incorporate unobservable inputs to determine fair market value.

The use of models and other valuation methods to determine fair market value often requires subjective and complex judgment. Actual results could differ from the results estimated through application of these methods.

See Note 13 for additional information about fair value measurements.

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COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Derivative Accounting

We are exposed to the impact of market fluctuations in the commodity price and transportation costs of electricity, natural gas, coal and in interest rates. We manage risks associated with market volatility by utilizing various physical and financial instruments including futures, forwards, options and swaps. As part of our overall risk management program, we may use derivative 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 transactions. We also enter into derivative instruments for economic hedging purposes. Contracts that have the same terms (quantities, delivery points and delivery periods) and for which power does not flow are netted, which reduces both revenues and fuel and purchased power expenses in our Consolidated Statements of Income, but does not impact our financial condition, net income or cash flows.

We account for our derivative contracts in accordance with derivatives and hedging guidance, which requires all derivatives not qualifying for a scope exception to be measured at fair value on the balance sheet as either assets or liabilities. Transactions with counterparties that have master netting arrangements are reported net on the balance sheet. See Notes 2 and 16 for additional information about our derivative instruments.

Loss Contingencies and Environmental Liabilities

Pinnacle West and APS are involved in certain legal and environmental matters that arise in the normal course of business. Contingent losses and environmental liabilities are recorded when it is determined that it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. When a range of the probable loss exists and no amount within the range is a better estimate than any other amount, Pinnacle West and APS record a loss contingency at the minimum amount in the range. Unless otherwise required by GAAP, legal fees are expensed as incurred.

Retirement Plans and Other Postretirement Benefits

Pinnacle West sponsors a qualified defined benefit and account balance pension plan for the employees of Pinnacle West and its subsidiaries. We also sponsor another postretirement benefit plan for the employees of Pinnacle West and its subsidiaries that provides medical and life insurance benefits to retired employees. Pension and other postretirement benefit

expense are determined by actuarial valuations, based on assumptions that are evaluated annually. See Note 7 for additional information on pension and other postretirement benefits. On January 1, 2018, we adopted new accounting guidance ASU 2017-07, Compensation-Retirement Benefits: Improving the presentation of net periodic pension cost and net periodic postretirement benefit cost. See Note 2 for additional discussion.

Nuclear Fuel

APS amortizes nuclear fuel by using the unit-of-production method. The unit-of-production method is based on actual physical usage. APS divides the cost of the fuel by the estimated number of thermal units it expects to produce with that fuel. APS then multiplies that rate by the number of thermal units produced within the current period. This calculation determines the current period nuclear fuel expense.

APS also charges nuclear fuel expense for the interim storage and permanent disposal of spent nuclear fuel. The DOE is responsible for the permanent disposal of spent nuclear fuel and charged APS \$0.001 per kWh of nuclear generation through May 2014, at which point the DOE reduced the fee to zero. In accordance with a settlement agreement with the DOE in August 2014, we will now accrue a receivable for incurred

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claims and an offsetting regulatory liability through the settlement period ending December of 2019. See Note 10 for information on spent nuclear fuel disposal costs.

Income Taxes

Income taxes are provided using the asset and liability approach prescribed by guidance relating to accounting for income taxes and are based on currently enacted tax rates. We file our federal income tax return on a consolidated basis, and we file our state income tax returns on a consolidated or unitary basis. In accordance with our intercompany tax sharing agreement, federal and state income taxes are allocated to each first-tier subsidiary as though each first-tier subsidiary filed a separate income tax return. Any difference between that method and the consolidated (and unitary) income tax liability is attributed to the parent company. The income tax accounts reflect the tax and interest associated with management's estimate of the largest amount of tax benefit that is greater than 50% likely of being realized upon settlement for all known and measurable tax exposures. On January 1, 2018, we adopted new guidance ASU 2018-02, Income Statement-Reporting Comprehensive Income: Reclassification of certain tax effects from accumulated other comprehensive income. See Note 4 for additional discussion.

Cash and Cash Equivalents

We consider cash equivalents to be highly liquid investments with a remaining maturity of three months or less at acquisition.

The following table summarizes supplemental Pinnacle West cash flow information for each of the last three years (dollars in thousands):

	Year ended December 31,		
	2018	2017	2016
Cash paid during the period for:			
Income taxes, net of refunds	\$21,173	\$2,186	\$9,956
Interest, net of amounts capitalized	208,479	189,288	184,462
Significant non-cash investing and financing activities:			
Accrued capital expenditures	\$132,620	\$130,404	\$114,855
Dividends declared but not paid	82,675	77,667	72,926
Sale of 4CA 7% interest in Four Corners	68,907	—	—

Intangible Assets

We have no goodwill recorded and have separately disclosed other intangible assets, primarily APS's software, on Pinnacle West's Consolidated Balance Sheets. The intangible assets are amortized over their finite useful lives. Amortization expense was \$68 million in 2018, \$72 million in 2017, and \$58 million in 2016. Estimated amortization expense on existing intangible assets over the next five years is \$58 million in 2019, \$47 million in 2020, \$34 million in 2021, \$25 million in 2022, and \$22 million in 2023. At December 31, 2018, the weighted-average remaining amortization period for intangible assets was 8 years.

Investments

El Dorado holds investments in both debt and equity securities. Investments in debt securities are generally accounted for as held-to-maturity and investments in equity securities are accounted for using either

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COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

the equity method (if significant influence) or the measurement alternative for investments without readily determinable fair values (if less than 20% ownership and no significant influence).

Our investments in the nuclear decommissioning trust fund, coal reclamation escrow and active union employee medical account, are accounted for in accordance with guidance on accounting for investments in debt and equity securities. See Notes 13 and 19 for more information on these investments.

On January 1, 2018, we adopted new accounting guidance ASU 2016-01, Financial Instruments: Recognition and measurement. See Note 2.

Business Segments

Pinnacle West's reportable business segment is our regulated electricity segment, which consists of traditional regulated retail and wholesale electricity businesses (primarily electricity service to Native Load customers) and related activities and includes electricity generation, transmission and distribution. All other segment activities are insignificant.

Preferred Stock

At December 31, 2018, Pinnacle West had 10 million shares of serial preferred stock authorized with no par value, none of which was outstanding, and APS had 15,535,000 shares of various types of preferred stock authorized with \$25, \$50 and \$100 par values, none of which was outstanding.

2. New Accounting Standards

Standards Adopted in 2018

ASU 2014-09, Revenue from Contracts with Customers

In May 2014, a new revenue recognition accounting standard was issued. This standard provides a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. Since the issuance of the new revenue standard, additional guidance was issued to clarify

certain aspects of the new revenue standard, including principal versus agent considerations, identifying performance obligations, and other narrow scope improvements. The new revenue standard, and related amendments, became effective for us on January 1, 2018. The standard may be adopted using a full retrospective application or a simplified transition method that allows entities to record a cumulative effect adjustment in retained earnings at the date of initial application.

We adopted this standard and related amendments on January 1, 2018 using the modified retrospective transition approach. The adoption of the new revenue guidance resulted in expanded disclosures, but otherwise did not have a material impact on our financial statements. See Note 20.

ASU 2016-01, Financial Instruments: Recognition and Measurement

In January 2016, a new accounting standard was issued relating to the recognition and measurement of financial instruments. The new guidance requires certain investments in equity securities to be measured at fair value with changes in fair value recognized in net income, and modifies the impairment assessment of certain equity securities. The new standard was effective for us on January 1, 2018. The standard required modified retrospective application, with the exception of certain aspects of the standard that required prospective

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

application. We adopted this standard on January 1, 2018, using primarily a retrospective approach. Due to regulatory accounting treatment, the adoption of this standard did not have a material impact on our financial statements. See Notes 13 and 19 for disclosures relating to our investments in debt and equity securities.

ASU 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments

In August 2016, a new accounting standard was issued that clarifies how entities should present certain specific cash flow activities on the statement of cash flows. The guidance is intended to eliminate diversity in practice in how entities classify these specific activities between cash flows from operating activities, investing activities and financing activities. The specific activities addressed include debt prepayments and extinguishment costs, proceeds from the settlement of insurance claims, proceeds from corporate-owned life insurance policies, and other activities. The standard also addresses how entities should apply the predominance principle when a transaction includes separately identifiable cash flows. The new standard was effective for us, and was adopted on January 1, 2018, using a retrospective transition method. The adoption of this guidance did not have a significant impact on our financial statements, as either our statement of cash flow presentation is consistent with the new prescribed guidance or we do not have significant activities relating to the specific transactions that are addressed by the new standard.

ASU 2016-18, Statement of Cash Flows: Restricted Cash

In November 2016, a new accounting standard was issued that clarifies how restricted cash and restricted cash equivalents should be presented on the statement of cash flows. The new guidance requires entities to include restricted cash and restricted cash equivalents as a component of the beginning and ending cash and cash equivalent balances on the statement of cash flows. The new standard is effective for us, and was adopted on January 1, 2018, using a retrospective transition method. The adoption of this guidance did not impact our financial statements, as our holdings and activities designated as restricted cash and restricted cash equivalents at transition and in prior periods are insignificant.

ASU 2017-01, Business Combinations: Clarifying the Definition of a Business

In January 2017, a new accounting standard was issued that clarifies the definition of a business. This standard is intended to assist entities with evaluating whether a transaction should be accounted for as an acquisition (or disposal) of assets or a business. The definition of a business affects many areas of accounting, including acquisitions, disposals, goodwill, and consolidation. The new standard was effective for us and was adopted on January 1, 2018 using a prospective transition approach. This standard did not have an impact on our financial statements on the date of adoption.

ASU 2017-05, Other Income: Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets

In February 2017, a new accounting standard was issued that intended to clarify the scope of accounting guidance pertaining to gains and losses from the derecognition of nonfinancial assets, and to add guidance for partial sales of nonfinancial assets. The new standard was effective for us, and was adopted on January 1, 2018, using a modified retrospective transition approach. This standard did not have a significant impact on our financial statements on the date of adoption. On July 3, 2018, 4CA sold its 7% interest in Four Corners. The sale transaction was accounted for in accordance with the guidance in ASU 2017-05, see Note 10.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ASU 2017-07, Compensation-Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

In March 2017, a new accounting standard was issued that modifies how plan sponsors present net periodic pension cost and net periodic postretirement benefit cost (net benefit costs). The presentation changes require net benefit costs to be disaggregated on the income statement by the various components that comprise these costs. Specifically, only the service cost component is eligible for presentation as an operating income item, and all other cost components are now presented as non-operating items. This presentation change was applied retrospectively. Furthermore, the new standard allows only the service cost component to be eligible for capitalization. The change in capitalization requirements was applied prospectively. The new guidance was effective for us on January 1, 2018.

We adopted this new accounting standard on January 1, 2018. As a result of adopting this standard we have presented the non-service cost components of net benefits costs in other income instead of operating income. Prior year non-service cost components have also been reclassified to conform to this new presentation. We elected to apply the practical expedient guidance. As such, prior period costs have been estimated based on amounts previously disclosed in our pension and other postretirement benefit plan notes. The changes impacting capitalization have been adopted prospectively. As such, upon adoption, we are no longer capitalizing a portion of the non-service cost components of net benefit costs.

In 2018 the non-service credit components are a reduction to total benefit costs. Excluding non-service credits from eligible capitalization costs resulted in the capitalization of an additional \$15 million of net benefit costs, with a corresponding increase to pretax income for the year. See Note 7 for additional information related to our pension plans and other postretirement benefits.

ASU 2018-02, Income Statement-Reporting Comprehensive Income: Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, new accounting guidance was issued that allows entities an optional election to reclassify the income tax effects of the Tax Act on items within accumulated other comprehensive income to retained earnings. Amounts eligible for reclassification must relate to the effects from the Tax Act remaining in accumulated other comprehensive income. The new guidance also requires expanded disclosures. This guidance is effective for

us on January 1, 2019 with early application permitted. The guidance should be applied either in the period of adoption or retrospectively to each period in which the effect of the Tax Act was recognized.

We early adopted this guidance in the quarter ended March 31, 2018, and we have elected to reclassify the income tax effects of the Tax Act related to other comprehensive income to retained earnings. As of December 31, 2018, on a consolidated basis our accumulated other comprehensive income decreased \$9 million, and APS's accumulated other comprehensive income decreased \$5 million, as a result of adopting this guidance. Amounts were reclassified from accumulated other comprehensive income to retained earnings, and related to tax rate changes. The adoption of this guidance did not impact our income from continuing operations. See Note 4 for additional discussion of the Tax Act.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS***Standards Adopted in 2019*****ASU 2016-02, Leases**

In February 2016, a new lease accounting standard was issued. This new standard supersedes the existing lease accounting model, and modifies both lessee and lessor accounting. The new standard requires a lessee to reflect most operating lease arrangements on the balance sheet by recording a right-of-use asset and a lease liability that is initially measured at the present value of lease payments. Among other changes, the new standard also modifies the definition of a lease, and requires expanded lease disclosures. Since the issuance of the new lease standard, additional lease related guidance has been issued relating to land easements and how entities may elect to account for these arrangements at transition, among other items. The new lease standard and related amendments were effective for us on January 1, 2019, with early application permitted. The standard must be adopted using a modified retrospective approach with a cumulative-effect adjustment to the opening balance of retained earnings determined at either the date of adoption, or the earliest period presented in the financial statements. The standard includes various optional practical expedients provided to facilitate transition.

We adopted this standard, and related amendments, on January 1, 2019. We elected the transition method that allows us to apply the guidance on the date of adoption, January 1, 2019, and will not retrospectively adjust prior periods. We also elected certain transition practical expedients that allow us to not reassess (a) whether any expired or existing contracts are or contain leases, (b) the lease classification for any expired or existing leases and (c) initial direct costs for any existing leases. These practical expedients apply to leases that commenced prior to January 1, 2019. Furthermore, we elected the practical expedient transition provisions relating to the treatment of existing land easements.

On January 1, 2019 the adoption of this new accounting standard resulted in the recognition on our Consolidated Balance Sheets of approximately \$194 million of right-of-use lease assets and \$119 million of lease liabilities relating to our operating lease arrangements. The right-of-use lease assets include \$85 million of prepaid lease costs that have been reclassified from other deferred debits, and \$10 million of deferred lease costs that have been reclassified from other current liabilities. In addition to these balance sheet impacts the adoption of the guidance will also result in expanded lease related disclosures in our 2019 financial statements.

ASU 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities

In August 2017, a new accounting standard was issued that modifies hedge accounting guidance with the intent of simplifying the application of hedge accounting. The new standard became effective for us on January 1, 2019, with early application permitted. At transition, the guidance requires the changes to be applied to hedging relationships existing on the date of adoption, with the effect of adoption reflected as of the beginning of the fiscal year of adoption using a cumulative effect adjustment approach. The presentation and disclosure changes may be applied prospectively. We adopted this standard on January 1, 2019 and because we are not currently applying hedge accounting, the adoption of the standard did not impact our financial statements.

Standards Pending Adoption

ASU 2016-13, Financial Instruments: Measurement of Credit Losses

In June 2016, a new accounting standard was issued that amends the measurement of credit losses on certain financial instruments. The new standard will require entities to use a current expected credit loss model

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to measure impairment of certain investments in debt securities, trade accounts receivables, and other financial instruments. The new standard is effective for us on January 1, 2020 and must be adopted using a modified retrospective approach for certain aspects of the standard, and a prospective approach for other aspects of the standard. We are currently evaluating this new accounting standard and the impacts it may have on our financial statements.

ASU 2018-15, Internal-Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract

In August 2018, a new accounting standard was issued that clarifies how customers in a cloud computing service arrangement should account for implementation costs associated with the arrangement. To determine which implementation costs should be capitalized, the new guidance aligns the accounting with existing guidance pertaining to internal-use software. As a result of this new standard, certain cloud computing service arrangement implementation costs will now be subject to capitalization and amortized on a straight-line basis over the cloud computing service arrangement term. The new standard is effective for us on January 1, 2020, with early application permitted, and may be applied using either a retrospective or prospective transition approach. We are currently evaluating this new accounting standard and the impacts it may have on our financial statements.

3. Regulatory Matters

Retail Rate Case Filing with the Arizona Corporation Commission

On June 1, 2016, APS filed an application with the ACC for an annual increase in retail base rates of \$165.9 million. This amount excluded amounts that were then collected on customer bills through adjustor mechanisms. The application requested that some of the balances in these adjustor accounts (aggregating to approximately \$267.6 million as of December 31, 2015) be transferred into base rates through the ratemaking process. This transfer would not have had an incremental effect on average customer bills. The average annual customer bill impact of APS's request was an increase of 5.74% (the average annual bill impact for a typical APS residential customer was 7.96%).

On March 27, 2017, a majority of the stakeholders in the general retail rate case, including the ACC Staff, the Residential Utility Consumer Office, limited income advocates and private rooftop solar organizations signed a settlement agreement (the "2017 Settlement

Agreement") and filed it with the ACC. The 2017 Settlement Agreement provides for a net retail base rate increase of \$94.6 million, excluding the transfer of adjustor balances, consisting of: (1) a non-fuel, non-depreciation, base rate increase of \$87.2 million per year; (2) a base rate decrease of \$53.6 million attributable to reduced fuel and purchased power costs; and (3) a base rate increase of \$61.0 million due to changes in depreciation schedules. The average annual customer bill impact under the 2017 Settlement Agreement was calculated as an increase of 3.28% (the average annual bill impact for a typical APS residential customer was calculated as 4.54%).

Other key provisions of the agreement include the following:

- an agreement by APS not to file another general retail rate case application before June 1, 2019;
- an authorized return on common equity of 10.0%;
- a capital structure comprised of 44.2% debt and 55.8% common equity;
- a cost deferral order for potential future recovery in APS's next general retail rate case for the construction and operating costs APS incurs for its Ocotillo modernization project;

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a cost deferral and procedure to allow APS to request rate adjustments prior to its next general retail rate case related to its share of the construction costs associated with installing selective catalytic reduction ("SCR") equipment at Four Corners;

a deferral for future recovery (or credit to customers) of the Arizona property tax expense above or below a specified test year level caused by changes to the applicable Arizona property tax rate;

an expansion of the PSA to include certain environmental chemical costs and third-party battery storage costs;

a new AZ Sun II program (now known as APS Solar Communities) for utility-owned solar DG with the purpose of expanding access to rooftop solar for low and moderate income Arizonans, recoverable through the RES, to be no less than \$10 million per year, and not more than \$15 million per year;

an increase to the per kWh cap for the environmental improvement surcharge from \$0.00016 to \$0.00050 and the addition of a balancing account;

rate design changes, including:

- a change in the on-peak time of use period from noon - 7 p.m. to 3 p.m. - 8 p.m. Monday through Friday, excluding holidays;
- non-grandfathered DG customers would be required to select a rate option that has time of use rates and either a new grid access charge or demand component;
- a Resource Comparison Proxy ("RCP") for exported energy of 2.9 cents per kWh in year one; and
- an agreement by APS not to pursue any new self-build generation (with certain exceptions) having an in-service date prior to January 1, 2022 (extended to December 31, 2027 for combined-cycle generating units), unless expressly authorized by the ACC.

Through a separate agreement, APS, industry representatives, and solar advocates committed to stand by the 2017 Settlement Agreement and refrain from seeking to undermine it through ballot initiatives, legislation or advocacy at the ACC.

On August 15, 2017, the ACC approved (by a vote of 4-1), the 2017 Settlement Agreement without material modifications. On August 18, 2017, the ACC issued a final written Opinion and Order reflecting its decision in APS's general retail rate case (the "2017 Rate Case Decision"), which is subject to requests for rehearing and potential appeal. The new rates went into effect on August 19, 2017.

On October 17, 2017, Warren Woodward (an intervener in APS's general retail rate case) filed a Notice of Appeal in the Arizona Court of Appeals, Division One. The notice raises a single issue related to the application of certain rate schedules to new APS residential customers after May 1, 2018. Mr. Woodward filed a second notice of appeal on November 13, 2017 challenging APS's \$5 per month automated metering infrastructure opt-out program. Mr. Woodward's two appeals have been consolidated, and APS requested and was granted intervention. Mr. Woodward filed his opening brief on March 28, 2018. The ACC and APS filed responsive briefs on June 21, 2018. The Arizona Court of Appeals issued a Memorandum Decision on December 11, 2018 affirming the ACC decisions challenged by Mr. Woodward. Mr. Woodward filed a petition for review with the Arizona Supreme Court on January 9, 2019. Review by the Arizona Supreme Court is discretionary. APS cannot predict the outcome of this consolidated appeal but does not believe it will have a material impact on our financial position, results of operations or cash flows.

On January 3, 2018, an APS customer filed a petition with the ACC that was determined by the ACC Staff to be a complaint filed pursuant to Arizona Revised Statute §40-246 (the "Complaint") and not a request for rehearing. Arizona Revised Statute §40-246 requires the ACC to hold a hearing regarding any complaint alleging that a public service corporation is in violation of any commission order or that the rates being charged are not just and reasonable if the complaint is signed by at least twenty-five customers of the public

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service corporation. The Complaint alleged that APS is “in violation of commission order” [sic]. On February 13, 2018, the complainant filed an amended Complaint alleging that the rates and charges in the 2017 Rate Case Decision are not just and reasonable. The complainant requested that the ACC hold a hearing on the amended Complaint to determine if the average bill impact on residential customers of the rates and charges approved in the 2017 Rate Case Decision is greater than 4.54% (the average annual bill impact for a typical APS residential customer estimated by APS,) and, if so, what effect the alleged greater bill impact has on APS's revenues and the overall reasonableness and justness of APS's rates and charges, in order to determine if there is sufficient evidence to warrant a full-scale rate hearing. The ACC held a hearing on this matter beginning in September 2018 and the hearing was concluded on October 1, 2018. Post-hearing briefing was concluded on December 14, 2018. APS expects a recommended opinion and order from the judge within the first quarter of 2019. APS cannot predict the outcome of this matter.

On December 24, 2018, certain ACC Commissioners filed a letter stating that because the ACC had received a substantial number of complaints that the rate increase authorized by the 2017 Rate Case Decision was much more than anticipated, they believe there is a possibility that APS is earning more than was authorized by the 2017 Rate Case Decision. Accordingly, the ACC Commissioners requested the ACC Staff to perform a rate review of APS using calendar year 2018 as a test year and file a report by May 3, 2019. The ACC Commissioners also asked the ACC Staff to evaluate APS's efforts to educate its customers regarding the new rates approved in the 2017 Rate Case Decision. On January 9, 2019, the ACC Commissioners voted to open a docket for this matter. APS does not believe that the rate review will have a material impact on our financial position, results of operations or cash flows. However, depending upon the results of the rate review, the ACC may take further actions, including potentially attempting to reopen the 2017 Rate Case Decision. APS cannot predict the outcome of this matter.

Prior Rate Case Filing with the Arizona Corporation Commission

On June 1, 2011, APS filed an application with the ACC for a net retail base rate increase of \$95.5 million. On January 6, 2012, APS and other parties to the general retail rate case entered into an agreement (the "2012 Settlement Agreement") detailing the terms upon which the parties agreed to settle the rate case. On May 15, 2012, the ACC approved the 2012 Settlement Agreement without material modifications.

Cost Recovery Mechanisms

APS has received regulatory decisions that allow for more timely recovery of certain costs outside of a general retail rate case through the following recovery mechanisms.

Renewable Energy Standard. In 2006, the ACC approved the 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 as part of 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 funding the upcoming year's RES budget.

In 2013, the ACC conducted a hearing to consider APS's proposal to establish compliance with distributed energy requirements by tracking and recording distributed energy, rather than acquiring and retiring renewable energy credits. On February 6, 2014, the ACC established a proceeding to modify the renewable energy rules to establish a process for compliance with the renewable energy requirement that is not based solely on the use of renewable energy credits. On September 9, 2014, the ACC authorized a rulemaking process to modify the RES rules. The proposed changes would permit the ACC to find that utilities have

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complied with the distributed energy requirement in light of all available information. The ACC adopted these changes on December 18, 2014. The revised rules went into effect on April 21, 2015.

In December 2014, the ACC voted that it had no objection to APS implementing an APS-owned rooftop solar research and development program aimed at learning how to efficiently enable the integration of rooftop solar and battery storage with the grid. The first stage of the program, called the "Solar Partner Program," placed 8 MW of residential rooftop solar on strategically selected distribution feeders in an effort to maximize potential system benefits, as well as made systems available to limited-income customers who could not easily install solar through transactions with third parties. The second stage of the program, which included an additional 2 MW of rooftop solar and energy storage, placed two energy storage systems sized at 2 MW on two different high solar penetration feeders to test various grid-related operation improvements and system interoperability, and was in operation by the end of 2016. The costs for this program have been included in APS's rate base as part of the 2017 Rate Case Decision.

On July 1, 2016, APS filed its 2017 RES Implementation Plan and proposed a budget of approximately \$150 million. APS's budget request included additional funding to process the high volume of residential rooftop solar interconnection requests and also requested a permanent waiver of the residential distributed energy requirement for 2017 contained in the RES rules. On April 7, 2017, APS filed an amended 2017 RES Implementation Plan and updated budget request which included the revenue neutral transfer of specific revenue requirements into base rates in accordance with the 2017 Settlement Agreement. On August 15, 2017, the ACC approved the 2017 RES Implementation Plan.

On June 30, 2017, APS filed its 2018 RES Implementation Plan and proposed a budget of approximately \$90 million. APS's budget request supports existing approved projects and commitments and includes the anticipated transfer of specific revenue requirements into base rates in accordance with the 2017 Settlement Agreement and also requests a permanent waiver of the residential distributed energy requirement for 2018 contained in the RES rules. APS's 2018 RES budget request is lower than the 2017 RES budget due in part to a certain portion of the RES being collected by APS in base rates rather than through the RES adjustor.

On November 20, 2017, APS filed an updated 2018 RES budget to include budget adjustments for APS Solar Communities (formerly known as AZ Sun II), which was approved as part of the 2017 Rate Case Decision. APS Solar Communities is a 3-year program authorizing APS to spend \$10 million to \$15 million in capital costs each year to install utility-owned DG systems for low to moderate income residential homes, buildings of non-profit entities, Title I schools and rural government facilities. The 2017 Rate Case Decision provided that all operations and maintenance expenses, property taxes, marketing and advertising expenses, and the capital carrying costs for this program will be recovered through the RES. On June 12, 2018, the ACC approved the 2018 RES Implementation Plan.

On June 29, 2018, APS filed its 2019 RES Implementation Plan and proposed a budget of approximately \$89.9 million. APS's budget request supports existing approved projects and commitments and requests a permanent waiver of the residential distributed energy requirement for 2019 contained in the RES rules. The ACC has not yet ruled on the 2019 RES Implementation Plan.

In September 2016, the ACC initiated a proceeding which will examine the possible modernization and expansion of the RES. On January 30, 2018, ACC Commissioner Tobin proposed a plan in this proceeding which would broaden the RES to include a series of energy policies tied to clean energy sources (the "Energy Modernization Plan"). The Energy Modernization Plan includes replacing the current RES standard with a new standard called the Clean Resource Energy Standard and Tariff ("CREST"), which incorporates the

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proposals in the Energy Modernization Plan. A set of draft CREST rules for the ACC's consideration was issued by Commissioner Tobin's office on July 5, 2018. See "Energy Modernization Plan" below for more information on CREST.

Demand Side Management Adjustor Charge. The ACC EES requires APS to submit a Demand Side Management Implementation Plan ("DSM Plan") annually for review by and approval of the ACC. On March 20, 2015, APS filed an application with the ACC requesting a budget of \$68.9 million for 2015 and minor modifications to its DSM portfolio going forward, including for the first time three resource savings projects which reflect energy savings on APS's system. The ACC approved APS's 2015 DSM budget on November 25, 2015. In its decision, the ACC also ruled that verified energy savings from APS's resource savings projects could be counted toward compliance with the EES; however, the ACC ruled that APS was not allowed to count savings from systems savings projects toward determination of the achievement of performance incentives, nor may APS include savings from conservation voltage reduction in the calculation of its LFCR mechanism.

On June 1, 2016, APS filed its 2017 DSM Plan, in which APS proposed programs and measures that specifically focus on reducing peak demand, shifting load to off-peak periods and educating customers about strategies to manage their energy and demand. The requested budget in the 2017 DSM Plan was \$62.6 million. On January 27, 2017, APS filed an updated and modified 2017 DSM Plan that incorporated the proposed Residential Demand Response, Energy Storage and Load Management Program and requested that the budget be increased to \$66.6 million. On August 15, 2017, the ACC approved the amended 2017 DSM Plan.

On September 1, 2017, APS filed its 2018 DSM Plan, which proposes modifications to the demand side management portfolio to better meet system and customer needs by focusing on peak demand reductions, storage, load shifting and demand response programs in addition to traditional energy savings measures. The 2018 DSM Plan seeks a reduced requested budget of \$52.6 million and requests a waiver of the EES for 2018. On November 14, 2017, APS filed an amended 2018 DSM Plan, which revised the allocations between budget items to address customer participation levels, but kept the overall budget at \$52.6 million. The ACC has not yet ruled on the APS 2018 amended DSM Plan.

On December 31, 2018, APS filed its 2019 DSM Plan, which requests a budget of \$34.1 million and continues APS's focus on DSM strategies such as peak demand reduction, load shifting, storage and electrification strategies. The ACC has not yet ruled on the APS 2019

DSM Plan.

Power Supply Adjustor Mechanism and Balance. The PSA provides for the adjustment of retail rates to reflect variations in retail fuel and purchased power costs. The PSA is subject to specified parameters and procedures, including the following:

- APS records deferrals for recovery or refund to the extent actual retail fuel and purchased power costs vary from the Base Fuel Rate;

- An adjustment to the PSA rate is made annually each February 1 (unless otherwise approved by the ACC) and goes into effect automatically unless suspended by the ACC;

The PSA uses a forward-looking estimate of fuel and purchased power costs to set the annual PSA rate, which is reconciled to actual costs experienced for each PSA Year (February 1 through January 31) (see the following bullet point);

The PSA rate includes (a) a “Forward Component,” under which APS recovers or refunds differences between expected fuel and purchased power costs for the upcoming calendar year

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and those embedded in the Base Fuel Rate; (b) a “Historical Component,” under which differences between actual fuel and purchased power costs and those recovered or refunded through the combination of the Base Fuel Rate and the Forward Component are recovered during the next PSA Year; and (c) a “Transition Component,” under which APS may seek mid-year PSA changes due to large variances between actual fuel and purchased power costs and the combination of the Base Fuel Rate and the Forward Component; and

• The PSA rate may not be increased or decreased more than \$0.004 per kWh in a year without permission of the ACC.

The following table shows the changes in the deferred fuel and purchased power regulatory asset (liability) for 2018 and 2017 (dollars in thousands):

	Twelve Months Ended December 31,	
	2018	2017
Beginning balance	\$ 75,637	\$ 12,465
Deferred fuel and purchased power costs — current period	78,277	48,405
Amounts refunded/(charged) to customers	(116,750)	14,767
Ending balance	\$ 37,164	\$ 75,637

The PSA rate for the PSA year beginning February 1, 2017 was \$(0.001348) per kWh, as compared to \$0.001678 per kWh for the prior year. This rate was comprised of a forward component of \$(0.001027) per kWh and a historical component of \$(0.000321) per kWh. On August 19, 2017, the PSA rate was revised to \$0.000555 per kWh as part of the 2017 Rate Case Decision. This new rate was comprised of a forward component of \$0.000876 per kWh and a historical component of \$(0.000321) per kWh.

The PSA rate for the PSA year beginning February 1, 2018 is \$0.004555 per kWh, consisting of a forward component of \$0.002009 per kWh and a historical component of \$0.002546 per kWh. This represented a \$0.004 per kWh increase over the August 19, 2017 PSA, the maximum permitted under the Plan of Administration for the PSA. This left \$16.4 million of 2017 fuel and purchased power costs above this annual cap. These costs rolled over until the following year and were reflected in the 2019 reset of the PSA.

On November 30, 2018, APS filed its PSA rate for the PSA year beginning February 1, 2019. That rate was \$0.001658 per kWh and consisted of a forward component of \$0.000536 per kWh and a historical component of \$0.001122 per kWh. The 2019 PSA rate is a

\$0.002897 per kWh decrease compared to 2018. These rates went into effect as filed on February 1, 2019.

Transmission Rates, Transmission Cost Adjustor and Other Transmission Matters. In July 2008, 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 and recover the costs that APS incurs in providing transmission services. A large portion of the rate represents charges for transmission services to serve APS's retail customers ("Retail Transmission Charges"). In order to recover the Retail Transmission Charges, APS was previously required to file an application with, and obtain approval from, the ACC to reflect changes in Retail Transmission Charges through the TCA. Under the terms of the 2012 Settlement Agreement, however, an adjustment to rates to recover the Retail Transmission Charges will be made annually each June 1 and will go into effect automatically unless suspended by the ACC.

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The formula rate is updated each year effective June 1 on the basis of APS's actual cost of service, as disclosed in APS's 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 could have a significant effect on the Retail Transmission Charges because any adjustment, though applied prospectively, may be calculated to account for previously over- or under-collected amounts.

Effective June 1, 2017, APS's annual wholesale transmission rates for all users of its transmission system increased by approximately \$35.1 million for the twelve-month period beginning June 1, 2017 in accordance with the FERC-approved formula. An adjustment to APS's retail rates to recover FERC approved transmission charges went into effect automatically on June 1, 2017. Effective June 1, 2018, APS's annual wholesale transmission rates for all users of its transmission system decreased by approximately \$22.7 million for the twelve-month period beginning June 1, 2018 in accordance with the FERC-approved formula. An adjustment to APS's retail rates to recover FERC approved transmission charges went into effect automatically on June 1, 2018.

On January 31, 2017, APS made a filing with FERC to reduce the Post-Employment Benefits Other than Pension expense reflected in its FERC transmission formula rate calculation to recognize certain savings resulting from plan design changes to the other postretirement benefit plans. A transmission customer intervened and protested certain aspects of APS's filing. FERC initiated a proceeding under Section 206 of the Federal Power Act to evaluate the justness and reasonableness of the revised formula rate filing APS proposed. APS entered into a settlement agreement with the intervening transmission customer, which was filed with FERC for approval on September 26, 2017. FERC approved the settlement agreement without modification or condition on December 21, 2017.

On March 7, 2018, APS made a filing to make modifications to its annual transmission formula to provide transmission customers the benefit of the reduced federal corporate income tax rate resulting from the Tax Act beginning in its 2018 annual transmission formula rate update filing. These modifications were approved by FERC on May 22, 2018

and reduced APS's transmission rates compared to the rate that would have gone into effect absent these changes.

Lost Fixed Cost Recovery Mechanism. The LFCR mechanism permits APS to recover on an after-the-fact basis a portion of its fixed costs that would otherwise have been collected by APS in the kWh sales lost due to APS energy efficiency programs and to DG such as rooftop solar arrays. The fixed costs recoverable by the LFCR mechanism were first established in the 2012 Settlement Agreement and amount to approximately 3.1 cents per residential kWh lost and 2.3 cents per non-residential kWh lost. These amounts were revised in the 2017 Settlement Agreement to 2.5 cents for both lost residential and non-residential kWh. The LFCR adjustment has a year-over-year cap of 1% of retail revenues. Any amounts left unrecovered in a particular year because of this cap can be carried over for recovery in a future year. The kWh's lost from energy efficiency are based on a third-party evaluation of APS's energy efficiency programs. DG sales losses are determined from the metered output from the DG units.

APS filed its 2016 annual LFCR adjustment on January 15, 2016, requesting an LFCR adjustment of \$46.4 million (a \$7.9 million annual increase). The ACC approved the 2016 annual LFCR effective beginning in May 2016. APS filed its 2017 LFCR adjustment on January 13, 2017 requesting an LFCR adjustment of

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\$63.7 million (a \$17.3 million per year increase over 2016 levels). On April 5, 2017, the ACC approved the 2017 annual LFCR adjustment as filed, effective with the first billing cycle of April 2017. On February 15, 2018, APS filed its 2018 annual LFCR Adjustment, requesting that effective May 1, 2018, the LFCR be adjusted to \$60.7 million (a \$3 million per year decrease from 2017 levels). On February 6, 2019, the ACC approved the 2018 annual LFCR adjustment to become effective March 1, 2019. On February 15, 2019, APS filed its 2019 annual LFCR adjustment, requesting that effective May 1, 2019, the annual LFCR recovery amount be reduced to \$36.2 million (a \$24.5 million decrease from previous levels). Because the LFCR mechanism has a balancing account that trues up any under or over recoveries, the delay in implementation does not have an adverse effect on APS.

Tax Expense Adjustor Mechanism and FERC Tax Filing. As part of the 2017 Settlement Agreement, the parties agreed to a rate adjustment mechanism to address potential federal income tax reform and enable the pass-through of certain income tax effects to customers. On December 22, 2017, the Tax Act was enacted. This legislation made significant changes to the federal income tax laws including a reduction in the corporate tax rate from 35% to 21% effective January 1, 2018.

On January 8, 2018, APS filed an application with the ACC requesting that the TEAM be implemented in two steps. The first addresses the change in the marginal federal tax rate from 35% to 21% resulting from the Tax Act and, if approved, would reduce rates by \$119.1 million annually through an equal cents per kWh credit. APS asked that this decrease become effective February 1, 2018. On February 22, 2018, the ACC approved the reduction of rates by \$119.1 million for the remainder of 2018 through an equal cents per kWh credit applied to all but a small subset of customers who are taking service under specially-approved tariffs. The rate reduction was effective for the first billing cycle in March 2018.

The impact of the TEAM, over time, is expected to be earnings neutral. However, on a quarterly basis, there is a difference between the timing and amount of the income tax benefit and the reduction in revenues refunded through the TEAM related to the lower federal income tax rate. The amount of the benefit of the lower federal income tax rate is based on quarterly pre-tax results, while the reduction in revenues from the prior year due to lower customer rates through the TEAM is based on a per kWh sales credit which follows our seasonal kWh sales pattern and is not impacted by earnings of the Company.

On August 13, 2018, APS filed a second request with the ACC to return an additional \$86.5 million in tax savings to customers. This second request addresses amortization of non-depreciation related excess deferred taxes previously collected from customers. The ACC has not yet approved this request.

Additionally, as part of this second request, APS informed the ACC of its intent to file a third future request to address the amortization of depreciation related excess deferred taxes, as the Company is currently in the process of seeking IRS guidance regarding the amortization method and period applicable to these depreciation related excess deferred taxes.

The TEAM expressly applies to APS's retail rates with the exception of a small subset of customers taking service under specially-approved tariffs noted above. As discussed under "Transmission Rates, Transmission Cost Adjustor and Other Transmission Matters" above, FERC issued an order on May 22, 2018 authorizing APS to provide for the cost reductions resulting from the income tax changes in its wholesale transmission rates.

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Net Metering

In 2015, the ACC voted to conduct a generic evidentiary hearing on the value and cost of DG to gather information that will inform the ACC on net metering issues and cost of service studies in upcoming utility rate cases. A hearing was held in April 2016. On October 7, 2016, the Administrative Law Judge issued a recommendation in the docket concerning the value and cost of DG solar installations. On December 20, 2016, the ACC completed its open meeting to consider the recommended opinion and order by the Administrative Law Judge. After making several amendments, the ACC approved the recommended decision by a 4-1 vote. As a result of the ACC's action, effective with APS's 2017 Rate Case Decision, the net metering tariff that governs payments for energy exported to the grid from residential rooftop solar systems was replaced by a more formula-driven approach that utilizes inputs from historical wholesale solar power until an avoided cost methodology is developed by the ACC.

As amended, the decision provides that payments by utilities for energy exported to the grid from DG solar facilities will be determined using a RCP methodology, a method that is based on the most recent five-year rolling average price that APS pays for utility-scale solar projects, while a forecasted avoided cost methodology is being developed. The price established by this RCP method will be updated annually (between general retail rate cases) but will not be decreased by more than 10% per year. Once the avoided cost methodology is developed, the ACC will determine in APS's subsequent rate cases which method (or a combination of methods) is appropriate to determine the actual price to be paid by APS for exported distributed energy.

In addition, the ACC made the following determinations:

- Customers who have interconnected a DG system or submitted an application for interconnection for DG systems prior to September 1, 2017, the date new rates were effective based on APS's 2017 Rate Case Decision, will be grandfathered for a period of 20 years from the date the customer's interconnection application was accepted by the utility;

- Customers with DG solar systems are to be considered a separate class of customers for ratemaking purposes; and

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Once an export price is set for APS, no netting or banking of retail credits will be available for new DG customers, and the then-applicable export price will be guaranteed for new customers for a period of 10 years.

This decision of the ACC addresses policy determinations only. The decision states that its principles will be applied in future general retail rate cases, and the policy determinations themselves may be subject to future change, as are all ACC policies. A first-year export energy price of 12.9 cents per kWh is included in the 2017 Settlement Agreement and became effective on September 1, 2017.

In accordance with the 2017 Rate Case Decision, APS filed its request for a second-year export energy price of 11.6 cents per kWh on May 1, 2018. This price reflects the 10% annual reduction discussed above. The new tariff became effective on October 1, 2018.

On January 23, 2017, TASC sought rehearing of the ACC's decision regarding the value and cost of DG. TASC asserted that the ACC improperly ignored the Administrative Procedure Act, failed to give adequate notice regarding the scope of the proceedings, and relied on information that was not submitted as evidence, among other alleged defects. TASC filed a Notice of Appeal in the Arizona Court of Appeals and filed a Complaint and Statutory Appeal in the Maricopa County Superior Court on March 10, 2017. As part of the

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2017 Settlement Agreement described above, TASC agreed to withdraw these appeals when the ACC decision implementing the 2017 Settlement Agreement is no longer subject to appellate review.

Subpoena from Arizona Corporation Commissioner Robert Burns

On August 25, 2016, Commissioner Burns, individually and not by action of the ACC as a whole, served subpoenas in APS's then current retail rate proceeding on APS and Pinnacle West for the production of records and information relating to a range of expenditures from 2011 through 2016. The subpoenas requested information concerning marketing and advertising expenditures, charitable donations, lobbying expenses, contributions to 501(c)(3) and (c)(4) nonprofits and political contributions. The return date for the production of information was set as September 15, 2016. The subpoenas also sought testimony from Company personnel having knowledge of the material, including the Chief Executive Officer.

On September 9, 2016, APS filed with the ACC a motion to quash the subpoenas or, alternatively to stay APS's obligations to comply with the subpoenas and decline to decide APS's motion pending court proceedings. Contemporaneously with the filing of this motion, APS and Pinnacle West filed a complaint for special action and declaratory judgment in the Superior Court of Arizona for Maricopa County, seeking a declaratory judgment that Commissioner Burns' subpoenas are contrary to law. On September 15, 2016, APS produced all non-confidential and responsive documents and offered to produce any remaining responsive documents that are confidential after an appropriate confidentiality agreement is signed.

On February 7, 2017, Commissioner Burns opened a new ACC docket and indicated that its purpose is to study and rectify problems with transparency and disclosure regarding financial contributions from regulated monopolies or other stakeholders who may appear before the ACC that may directly or indirectly benefit an ACC Commissioner, a candidate for ACC Commissioner, or key ACC Staff. As part of this docket, Commissioner Burns set March 24, 2017 as a deadline for the production of all information previously requested through the subpoenas. Neither APS nor Pinnacle West produced the information requested and instead objected to the subpoena. On March 10, 2017, Commissioner Burns filed suit against APS and Pinnacle West in the Superior Court of Arizona for Maricopa County in an effort to enforce his subpoenas. On March 30, 2017, APS filed a motion to dismiss Commissioner

Burns' suit against APS and Pinnacle West. In response to the motion to dismiss, the court stayed the suit and ordered Commissioner Burns to file a motion to compel the production of the information sought by the subpoenas with the ACC. On June 20, 2017, the ACC denied the motion to compel.

On August 4, 2017, Commissioner Burns amended his complaint to add all of the ACC Commissioners and the ACC itself as defendants. All defendants moved to dismiss the amended complaint. On February 15, 2018, the Superior Court dismissed Commissioner Burns' amended complaint. On March 6, 2018, Commissioner Burns filed an objection to the proposed final order from the Superior Court and a motion to further amend his complaint. The Superior Court permitted Commissioner Burns to amend his complaint to add a claim regarding his attempted investigation into whether his fellow commissioners should have been disqualified from voting on APS's 2017 rate case. Commissioner Burns filed his second amended complaint, and all defendants filed responses opposing the second amended complaint and requested that it be dismissed. Oral argument occurred in November 2018 regarding the motion to dismiss. On December 18, 2018, the trial court granted the defendants' motions to dismiss and entered final judgment on January 18, 2019. On February 13, 2019, Commissioner Burns filed a notice of appeal. APS and Pinnacle West cannot predict the outcome of this matter.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Renewable Energy Ballot Initiative

On February 20, 2018, a renewable energy advocacy organization filed with the Arizona Secretary of State a ballot initiative for an Arizona constitutional amendment requiring Arizona public service corporations to provide at least 50% of their annual retail sales of electricity from renewable sources by 2030. For purposes of the proposed amendment, eligible renewable sources would not include nuclear generating facilities. The initiative was placed on the November 2018 Arizona elections ballot. On November 6, 2018, the initiative failed to receive adequate voter support and was defeated.

Energy Modernization Plan

On January 30, 2018, ACC Commissioner Tobin proposed the Energy Modernization Plan, which consists of a series of energy policies tied to clean energy sources such as energy storage, biomass, energy efficiency, electric vehicles, and expanded energy planning through the IRP process. The Energy Modernization Plan includes replacing the current RES standard with a new standard called the CREST, which incorporates the proposals in the Energy Modernization Plan. On February 22, 2018, the ACC Staff filed a Notice of Inquiry to further examine the matter. As a part of this proposal, the ACC voted in March 2018 to direct utilities to develop a comprehensive biomass generation plan to be included in each utility's RES Implementation Plan. On July 5, 2018, Commissioner Tobin's office issued a set of draft CREST rules for the ACC's consideration.

In August 2018, the ACC directed ACC Staff to open a new rulemaking docket which will address a wide range of energy issues, including the Energy Modernization Plan proposals. The rulemaking will consider possible modifications to existing ACC rules, such as the Renewable Energy Standard, Electric and Gas Energy Efficiency Standards, Net Metering, Resource Planning, and the Biennial Transmission Assessment, as well as the development of new rules regarding forest bioenergy, electric vehicles, interconnection of distributed generation, baseload security, blockchain technology and other technological developments, retail competition, and other energy-related topics. Workshops on these energy issues are scheduled to be held throughout 2019. APS cannot predict the outcome of this matter.

Integrated Resource Planning

ACC rules require utilities to develop fifteen-year IRPs which describe how the utility plans to serve customer load in the plan timeframe. The ACC reviews each utility's IRP to

determine if it meets the necessary requirements and whether it should be acknowledged. In March of 2018, the ACC reviewed the 2017 IRPs of its jurisdictional utilities and voted to not acknowledge any of the plans. APS does not believe that this lack of acknowledgment will have a material impact on our financial position, results of operations or cash flows. Based on an ACC decision, APS is required to file a Preliminary Resource Plan by April 1, 2019 and its final IRP by April 1, 2020.

Four Corners

SCE-Related Matters. On December 30, 2013, APS purchased SCE's 48% ownership interest in each of Units 4 and 5 of Four Corners. The 2012 Settlement Agreement includes a procedure to allow APS to request rate adjustments prior to its next general retail rate case related to APS's acquisition of the additional interests in Units 4 and 5 and the related closure of Units 1-3 of Four Corners. APS made its filing under this provision on December 30, 2013. On December 23, 2014, the ACC approved rate adjustments resulting in a revenue increase of \$57.1 million on an annual basis. This included the deferral for future recovery of all non-fuel operating costs for the acquired SCE interest in Four Corners, net of the non-fuel operating costs savings

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resulting from the closure of Units 1-3 from the date of closing of the purchase through its inclusion in rates. The 2012 Settlement Agreement also provided for deferral for future recovery of all unrecovered costs incurred in connection with the closure of Units 1-3. The deferral balance related to the acquisition of SCE's interest in Units 4 and 5 and the closure of Units 1-3 was \$48 million as of December 31, 2018 and is being amortized in rates over a total of 10 years. The ACC's rate adjustment decision was appealed and on September 26, 2017, the Court of Appeals affirmed the ACC's decision on the Four Corners rate adjustment.

As part of APS's acquisition of SCE's interest in Units 4 and 5, APS and SCE agreed, via a "Transmission Termination Agreement" that, upon closing of the acquisition, the companies would terminate an existing transmission agreement ("Transmission Agreement") between the parties that provides transmission capacity on a system (the "Arizona Transmission System") for SCE to transmit its portion of the output from Four Corners to California. APS previously submitted a request to FERC related to this termination, which resulted in a FERC order denying rate recovery of \$40 million that APS agreed to pay SCE associated with the termination. On December 22, 2015, APS and SCE agreed to terminate the Transmission Termination Agreement and allow for the Transmission Agreement to expire according to its terms, which includes settling obligations in accordance with the terms of the Transmission Agreement. APS established a regulatory asset of \$12 million in 2015 in connection with the payment required under the terms of the Transmission Agreement. On July 1, 2016, FERC issued an order denying APS's request to recover the regulatory asset through its FERC-jurisdictional rates. APS and SCE completed the termination of the Transmission Agreement on July 6, 2016. APS made the required payment to SCE and wrote-off the \$12 million regulatory asset and charged operating revenues to reflect the effects of this order in the second quarter of 2016. On July 29, 2016, APS filed a request for rehearing with FERC. In its order denying recovery, FERC also referred to its enforcement division a question of whether the agreement between APS and SCE relating to the settlement of obligations under the Transmission Agreement was a jurisdictional contract that should have been filed with FERC. On October 5, 2017, FERC issued an order denying APS's request for rehearing. FERC also upheld its prior determination that the agreement relating to the settlement was a jurisdictional contract and should have been filed with FERC. APS cannot predict whether or if the enforcement division will take any action. APS filed an appeal of FERC's July 1, 2016 and October 5, 2017 orders with the United States Court of Appeals for the Ninth Circuit on December 4, 2017. That proceeding is pending, and APS cannot predict the outcome of the proceeding.

SCR Cost Recovery. On December 29, 2017, in accordance with the 2017 Rate Case Decision, APS filed a Notice of Intent to file its SCR Adjustment to permit recovery of costs associated with the installation of SCR equipment at Four Corners Units 4 and 5. APS filed the SCR Adjustment request in April 2018. Consistent with the 2017 Rate Case Decision, the request was narrow in scope and addressed only costs associated with this specific environmental compliance equipment. The SCR Adjustment request provided that there would be a \$67.5 million annual revenue impact that would be applied as a percentage of base rates for all applicable customers. Also, as provided for in the 2017 Rate Case Decision, APS requested that the adjustment become effective no later than January 1, 2019. The hearing for this matter occurred in September 2018. At the hearing, APS accepted ACC Staff's recommendation of a lower annual revenue impact of approximately \$58.5 million. The Administrative Law Judge issued a Recommended Opinion and Order finding that the costs for the SCR project were prudently incurred and recommending authorization of the \$58.5 million annual revenue requirement related to the installation and operation of the SCRs. Exceptions to the Recommended Opinion and Order were filed by the parties and intervenors on December 7, 2018. The ACC has not issued a decision on this matter. APS anticipates a decision later in 2019.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Cholla

On September 11, 2014, APS announced that it would close Unit 2 of Cholla and cease burning coal at the other APS-owned units (Units 1 and 3) at the plant by the mid-2020s, if EPA approves a compromise proposal offered by APS to meet required environmental and emissions standards and rules. On April 14, 2015, the ACC approved APS's plan to retire Unit 2, without expressing any view on the future recoverability of APS's remaining investment in the Unit. APS closed Unit 2 on October 1, 2015. In early 2017, EPA approved a final rule incorporating APS's compromise proposal, which took effect on April 26, 2017.

Previously, APS estimated Cholla Unit 2's end of life to be 2033. APS has been recovering a return on and of the net book value of the unit in base rates. Pursuant to the 2017 Settlement Agreement described above, APS will be allowed continued recovery of the net book value of the unit and the unit's decommissioning and other retirement-related costs (\$89 million as of December 31, 2018), in addition to a return on its investment. In accordance with GAAP, in the third quarter of 2014, Unit 2's remaining net book value was reclassified from property, plant and equipment to a regulatory asset. The 2017 Settlement Agreement also shortened the depreciation lives of Cholla Units 1 and 3 to 2026.

Navajo Plant

The co-owners of the Navajo Plant and the Navajo Nation agreed that the Navajo Plant will remain in operation until December 2019 under the existing plant lease. The co-owners and the Navajo Nation executed a lease extension on November 29, 2017 that will allow for decommissioning activities to begin after the plant ceases operations in December 2019. Various stakeholders including regulators, tribal representatives, the plant's coal supplier and the U.S. Department of the Interior have been meeting to determine if an alternate solution can be reached that would permit continued operation of the plant beyond 2019. Although we cannot predict whether any alternate plans will be found that would be acceptable to all of the stakeholders and feasible to implement, we believe it is probable that the current owners of the Navajo Plant will cease operations in December 2019.

On February 14, 2017, the ACC opened a docket titled "ACC Investigation Concerning the Future of the Navajo Generating Station" with the stated goal of engaging stakeholders and negotiating a sustainable pathway for the Navajo Plant to continue operating in some form after December 2019. APS cannot predict the outcome of this proceeding.

APS is currently recovering depreciation and a return on the net book value of its interest in the Navajo Plant over its previously estimated life through 2026. APS will seek continued recovery in rates for the book value of its remaining investment in the plant (\$88 million as of December 31, 2018) plus a return on the net book value as well as other costs related to retirement and closure, which are still being assessed and may be material. APS believes it will be allowed recovery of the net book value, in addition to a return on its investment. In accordance with GAAP, in the second quarter of 2017, APS's remaining net book value of its interest in the Navajo Plant was reclassified from property, plant and equipment to a regulatory asset. If the ACC does not allow full recovery of the remaining net book value of this interest, all or a portion of the regulatory asset will be written off and APS's net income, cash flows, and financial position will be negatively impacted.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Regulatory Assets and Liabilities**

The detail of regulatory assets is as follows (dollars in thousands):

	Amortization Through	December 31, 2018		December 31, 2017	
		Current	Non-Current	Current	Non-Current
Pension	(a)	\$—	\$733,351	\$—	\$576,188
Retired power plant costs	2033	28,182	167,164	27,402	188,843
Income taxes - AFUDC equity	2048	6,457	151,467	3,828	142,852
Deferred fuel and purchased power — mark-to-market (Note 16)	2023	31,728	23,768	52,100	34,845
Deferred fuel and purchased power (b) (c)	2019	37,164	—	75,637	—
Four Corners cost deferral	2024	8,077	40,228	8,077	48,305
Income taxes — investment tax credit basis adjustment	2047	1,079	25,522	1,066	26,218
Lost fixed cost recovery (b)	2019	32,435	—	59,844	—
Palo Verde VIEs (Note 18)	2046	—	20,015	—	19,395
Deferred compensation	2036	—	36,523	—	36,413
Deferred property taxes	2027	8,569	66,356	8,569	74,926
Loss on reacquired debt	2038	1,637	13,668	1,637	15,305
Tax expense of Medicare subsidy	2024	1,235	6,176	1,236	7,415
TCA balancing account (b)	2020	3,860	772	1,220	—
AG-1 deferral	2022	2,654	5,819	2,654	8,472
Mead-Phoenix transmission line CIAC	2050	332	10,044	332	10,376
Coal reclamation	2026	1,546	15,607	1,068	12,396
SCR deferral	N/A	—	23,276	—	353
Other	Various	1,947	3,185	3,418	—
Total regulatory assets (d)		\$166,902	\$1,342,941	\$248,088	\$1,202,302

This asset represents the future recovery of pension benefit obligations through retail (a) rates. If these costs are disallowed by the ACC, this regulatory asset would be charged to OCI and result in lower future revenues. See Note 7 for further discussion.

(b) See “Cost Recovery Mechanisms” discussion above.

(c) Subject to a carrying charge.

(d) There are no regulatory assets for which the ACC has allowed recovery of costs, but not allowed a return by exclusion from rate base. FERC rates are set using a formula rate as described in “Transmission Rates, Transmission Cost Adjustor and Other Transmission Matters.”

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The detail of regulatory liabilities is as follows (dollars in thousands):

	Amortization Through	December 31, 2018		December 31, 2017	
		Current	Non-Current	Current	Non-Current
Excess deferred income taxes - ACC - Tax Cuts and Jobs Act	(a)	\$—	\$1,272,709	\$—	\$1,266,104
Excess deferred income taxes - FERC - Tax Cuts and Jobs Act	2058	6,302	243,691	—	254,170
Asset retirement obligations	2057	—	278,585	—	332,171
Removal costs	(b)	39,866	177,533	18,238	209,191
Other post retirement benefits	(c)	37,864	125,903	37,642	151,985
Income taxes - deferred investment tax credit	2047	2,164	51,120	2,164	52,497
Income taxes - change in rates	2048	2,769	70,069	2,573	70,537
Spent nuclear fuel	2027	6,503	57,002	6,924	62,132
Renewable energy standard (d)	2020	44,966	20	23,155	—
Demand side management (d)	2020	14,604	4,123	3,066	4,921
Sundance maintenance	2030	1,278	17,228	—	16,897
Deferred gains on utility property	2022	4,423	6,581	4,423	10,988
Four Corners coal reclamation	2038	1,858	17,871	1,858	18,921
Tax expense adjustor mechanism (d)	2019	3,237	—	—	—
Other	Various	42	3,541	43	2,022
Total regulatory liabilities		\$165,876	\$2,325,976	\$100,086	\$2,452,536

(a) While the majority of the excess deferred tax balance shown is subject to special amortization rules under federal income tax laws, which require amortization of the balance over the remaining regulatory life of the related property, treatment of a portion of the liability, and the month in which pass-through of the excess deferred tax balance will begin is subject to regulatory approval. This approval will be sought through the Company's TEAM adjustor mechanism. As a result, the Company cannot estimate the amount of this regulatory liability which is expected to reverse within the next 12 months. See Note 4.

(b) In accordance with regulatory accounting guidance, APS accrues for removal costs for its regulated assets, even if there is no legal obligation for removal.

(c) See Note 7.

(d) See “Cost Recovery Mechanisms” discussion above.

4. Income Taxes

Certain assets and liabilities are reported differently for income tax purposes than they are for financial statement purposes. The tax effect of these differences is recorded as deferred

taxes. We calculate deferred taxes using currently enacted income tax rates.

APS has recorded regulatory assets and regulatory liabilities related to income taxes on its Balance Sheets in accordance with accounting guidance for regulated operations. The regulatory assets are for certain temporary differences, primarily the allowance for equity funds used during construction, investment tax credit (“ITC”) basis adjustment and tax expense of Medicare subsidy. The regulatory liabilities primarily relate to the change in income tax rates and deferred taxes resulting from ITCs.

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COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On December 22, 2017, the Tax Act was enacted. This legislation made significant changes to the federal income tax laws, including a reduction in the corporate tax rate to 21% effective January 1, 2018. As a result of this rate reduction, the Company recognized a \$1.14 billion reduction in its net deferred income tax liabilities as of December 31, 2017.

In accordance with accounting for regulated companies, the effect of this rate reduction is substantially offset by a net regulatory liability. As of December 31, 2017, to reflect the **\$1.14 billion** reduction in its net deferred income tax liabilities caused by the rate reduction, APS has recorded a net regulatory liability of \$1.52 billion and a new \$377 million net deferred tax asset. The Company will amortize the net regulatory liability in accordance with applicable federal income tax laws, which require the amortization of a majority of the balance over the remaining regulatory life of the related property. As a result of the modifications made to the annual transmission formula rate during the second quarter, the Company has recorded amortization of FERC jurisdictional net excess deferred tax liabilities, retroactive to January 1, 2018. The Company continues to work with the ACC on a plan to amortize the remaining net excess deferred tax liabilities subject to its jurisdiction. See Note 3 for more details.

In August 2018, Treasury proposed regulations that clarify bonus depreciation transition rules under the Tax Act for regulated public utility property placed in service after September 27, 2017 and before January 1, 2018. During the third quarter the Company recorded deferred tax liabilities of approximately \$11 million and an increase in its net regulatory liability for excess deferred taxes of approximately \$9 million, primarily related to bonus depreciation benefits claimed on the Company's 2017 tax return as a result of this clarifying guidance. However, the proposed regulations are ambiguous with respect to regulated public utility property placed in service on or after January 1, 2018. On December 20, 2018, the Joint Committee on Taxation ("JCT") released the general explanation of the Tax Act. The document - commonly referred to as the "Blue Book" - provides a comprehensive technical description of the Tax Act and includes the legislative intent of Congress with respect to the changes made by provisions of the Tax Act. The "Blue Book" provides clarification that the intent of the Tax Act was to exclude from the definition of bonus depreciation qualified property any property placed in service by a regulated public utility after December 31, 2017. In a footnote, the JCT indicated that a technical correction bill may be necessary to reflect this intent.

Management recognizes tax positions which it believes are "more likely than not" to be sustained upon examination. In applying this "more likely than not" assessment, the Company is required to consider the technical merits of a position, including legislative intent. As a result, while no legislation has been passed which clarifies the ambiguities related to bonus depreciation for property placed in service on or after January 1, 2018, the Company currently believes the continued availability of bonus depreciation is not "more likely than not" to be sustained upon examination. As a result, the Company has not recognized any current or deferred tax benefits related to bonus depreciation for property placed in service on or after January 1, 2018.

For the quarter ending March 31, 2018, the Company early adopted ASU 2018-02, Income Statement-Reporting Comprehensive Income: Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income and elected to reclassify the income tax effects of the Tax Act on items within accumulated other comprehensive income to retained earnings. See Note 2 for additional information.

In accordance with regulatory requirements, APS ITCs are deferred and are amortized over the life of the related property with such amortization applied as a credit to reduce current income tax expense in the statement of income.

Net income associated with the Palo Verde sale leaseback VIEs is not subject to tax (see Note 18). As a result, there is no income tax expense associated with the VIEs recorded on the Pinnacle West Consolidated and APS Consolidated Statements of Income.

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The following is a tabular reconciliation of the total amounts of unrecognized tax benefits, excluding interest and penalties, at the beginning and end of the year that are included in accrued taxes and unrecognized tax benefits (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	2018	2017	2016	2018	2017	2016
Total unrecognized tax benefits, January 1	\$41,966	\$36,075	\$34,447	\$41,966	\$36,075	\$34,447
Additions for tax positions of the current year	3,436	2,937	2,695	3,436	2,937	2,695
Additions for tax positions of prior years	2,696	4,783	886	2,696	4,783	886
Reductions for tax positions of prior years for:						
Changes in judgment	(1,764)	(1,829)	(1,953)	(1,764)	(1,829)	(1,953)
Settlements with taxing authorities	—	—	—	—	—	—
Lapses of applicable statute of limitations	(5,603)	—	—	(5,603)	—	—
Total unrecognized tax benefits, December 31	\$40,731	\$41,966	\$36,075	\$40,731	\$41,966	\$36,075

Included in the balances of unrecognized tax benefits are the following tax positions that, if recognized, would decrease our effective tax rate (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	2018	2017	2016	2018	2017	2016
Tax positions, that if recognized, would decrease our effective tax rate	\$19,504	\$16,373	\$11,313	\$19,504	\$16,373	\$11,313

As of the balance sheet date, the tax year ended December 31, 2015 and all subsequent tax years remain subject to examination by the IRS. With a few exceptions, we are no longer subject to state income tax examinations by tax authorities for years before 2014.

We reflect interest and penalties, if any, on unrecognized tax benefits in the Pinnacle West Consolidated and APS Consolidated Statements of Income as income tax expense. The amount of interest expense or benefit recognized related to unrecognized tax benefits are as follows (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	2018	2017	2016	2018	2017	2016
Unrecognized tax benefit interest expense/(benefit) recognized	\$(780)	\$577	\$529	\$(780)	\$577	\$529

Following are the total amount of accrued liabilities for interest recognized related to unrecognized benefits that could reverse and decrease our effective tax rate to the extent matters are settled favorably (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	2018	2017	2016	2018	2017	2016
Unrecognized tax benefit interest accrued	\$1,130	\$1,910	\$1,333	\$1,130	\$1,910	\$1,333

Additionally, as of December 31, 2018, we have recognized less than \$1 million of interest expense to be paid on the underpayment of income taxes for certain adjustments that we have filed, or will file, with the IRS.

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The components of income tax expense are as follows (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	Year Ended December 31,			Year Ended December 31,		
	2018	2017	2016	2018	2017	2016
Current:						
Federal	\$18,375	\$11,624	\$8,630	\$88,180	\$21,512	\$711
State	3,342	3,052	1,259	1,877	2,778	4,276
Total current	21,717	14,676	9,889	90,057	24,290	4,987
Deferred:						
Federal	94,721	223,729	201,743	32,436	221,078	215,178
State	17,464	19,867	24,779	22,321	23,800	25,677
Total deferred	112,185	243,596	226,522	54,757	244,878	240,855
Income tax expense	\$133,902	\$258,272	\$236,411	\$144,814	\$269,168	\$245,842

The following chart compares pretax income at the statutory federal income tax rate of 21% in 2018 and 35% in 2017 and 2016 to income tax expense (dollars in thousands):

	Pinnacle West Consolidated			APS Consolidated		
	Year Ended December 31,			Year Ended December 31,		
	2018	2017	2016	2018	2017	2016
Federal income tax expense at statutory rate	\$139,533	\$268,177	\$244,278	\$154,260	\$277,540	\$254,617
Increases (reductions) in tax expense resulting from:						
State income tax net of federal income tax benefit	16,411	14,897	16,311	19,091	17,276	18,750
Nondeductible expenditures associated with ballot initiative	7,879	—	—	—	—	—
Stock compensation	(1,804)	(6,659)	(2,951)	(780)	(3,489)	(1,937)
Excess deferred income taxes - Tax Cuts and Jobs Act	(6,725)	9,348	—	(4,715)	9,431	—
Allowance for equity funds used during construction (see Note 1)	(7,231)	(12,937)	(11,724)	(7,231)	(12,937)	(11,724)
Palo Verde VIE noncontrolling interest (see Note 18)	(4,094)	(6,823)	(6,823)	(4,094)	(6,823)	(6,823)
Investment tax credit amortization	(6,742)	(6,715)	(5,887)	(6,742)	(6,715)	(5,887)
Other	(3,325)	(1,016)	3,207	(4,975)	(5,115)	(1,154)
Income tax expense	\$133,902	\$258,272	\$236,411	\$144,814	\$269,168	\$245,842

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The components of the net deferred income tax liability were as follows (dollars in thousands):

	Pinnacle West Consolidated		APS Consolidated	
	December 31,		December 31,	
	2018	2017	2018	2017
DEFERRED TAX ASSETS				
Risk management activities	\$15,785	\$25,103	\$15,785	\$25,103
Regulatory liabilities:				
Excess deferred income taxes - Tax Cuts and Jobs Act	376,869	376,906	376,869	376,906
Asset retirement obligation and removal costs	117,201	135,847	117,201	135,847
Unamortized investment tax credits	53,284	54,661	53,284	54,661
Other postretirement benefits	40,532	47,021	40,532	47,021
Other	40,380	37,489	40,380	37,489
Pension liabilities	112,019	83,126	107,009	77,280
Coal reclamation liabilities	47,508	45,802	47,508	45,802
Renewable energy incentives	30,779	33,546	30,779	33,546
Credit and loss carryforwards	1,755	53,946	—	1,920
Other	58,820	56,630	59,919	62,421
Total deferred tax assets	894,932	950,077	889,266	897,996
DEFERRED TAX LIABILITIES				
Plant-related	(2,277,724)	(2,220,886)	(2,277,724)	(2,220,886)
Risk management activities	(237)	(491)	(237)	(491)
Other postretirement assets and other special use funds	(57,697)	(66,134)	(57,274)	(65,733)
Regulatory assets:				
Allowance for equity funds used during construction	(39,086)	(36,365)	(39,086)	(36,365)
Deferred fuel and purchased power	(23,086)	(40,778)	(23,086)	(40,778)
Pension benefits	(181,504)	(142,848)	(181,504)	(142,848)
Retired power plant costs (see Note 3)	(48,348)	(53,611)	(48,348)	(53,611)
Other	(72,096)	(74,423)	(72,096)	(74,423)
Other	(2,575)	(5,346)	(2,575)	(5,346)
Total deferred tax liabilities	(2,702,353)	(2,640,882)	(2,701,930)	(2,640,481)
Deferred income taxes — net	\$(1,807,421)	\$(1,690,805)	\$(1,812,664)	\$(1,742,485)

As of December 31, 2018, the deferred tax assets for credit and loss carryforwards relate primarily to federal general business credits of approximately \$14 million, which first begin to expire in 2036, and state credit carryforwards net of federal benefit of \$7 million, which first begin to expire in 2023. The credit and loss carryforwards amount above has been reduced by \$19 million of unrecognized tax benefits.

5. Lines of Credit and Short-Term Borrowings

Pinnacle West and APS maintain committed revolving credit facilities in order to enhance liquidity and provide credit support for their commercial paper programs, to refinance

indebtedness, and for other general corporate purposes.

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The table below presents the consolidated credit facilities and the amounts available and outstanding as of December 31, 2018 and 2017 (dollars in thousands):

	December 31, 2018			December 31, 2017		
	Pinnacle West	APS	Total	Pinnacle West	APS	Total
Commitments under Credit Facilities	\$350,000	\$1,000,000	\$1,350,000	\$325,000	\$1,000,000	\$1,325,000
Outstanding Commercial Paper and Revolving Credit Facility Borrowings	(76,400)	—	(76,400)	(95,400)	—	(95,400)
Amount of Credit Facilities Available	\$273,600	\$1,000,000	\$1,273,600	\$229,600	\$1,000,000	\$1,229,600
Weighted-Average Commitment Fees	0.125%	0.100%		0.125%	0.100%	

Pinnacle West

On June 28, 2018, Pinnacle West refinanced its 364-day \$125 million unsecured revolving credit facility that would have matured on July 30, 2018 with a new 364-day \$150 million credit facility that matures June 27, 2019. Borrowings under the facility bear interest at LIBOR plus 0.70% per annum. At December 31, 2018, Pinnacle West had \$54 million outstanding under the facility.

On July 12, 2018, Pinnacle West replaced its \$200 million revolving credit facility that would have matured in May 2021, with a new \$200 million facility that matures in July 2023. 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. At December 31, 2018, Pinnacle West had no outstanding borrowings under its credit facility, no letters of credit outstanding and \$22 million of commercial paper borrowings.

APS

On July 12, 2018, APS replaced its \$500 million revolving credit facility that would have matured in May 2021, with a new \$500 million facility that matures in July 2023.

At December 31, 2018, APS had two revolving credit facilities totaling \$1 billion, including a \$500 million credit facility that matures in June 2022 and the above-mentioned \$500 million facility. APS may increase the amount of each facility up to a maximum of \$700 million, for a total of \$1.4 billion, upon the satisfaction of certain conditions and with the

consent of the lenders. Interest rates are based on APS's senior unsecured debt credit ratings. These facilities are available to support APS's \$500 million commercial paper program, for bank borrowings or for issuances of letters of credit. At December 31, 2018, APS had no commercial paper outstanding and no outstanding borrowings or letters of credit under its revolving credit facilities. See "Financial Assurances" in Note 10 for a discussion of APS's other outstanding letters of credit.

Debt Provisions

On November 27, 2018, the ACC issued a financing order in which, subject to specified parameters and procedures, it approved APS's short-term debt authorization equal to a sum of (i) 7% of APS's capitalization, and (ii) \$500 million (which is required to be used for costs relating to purchases of natural gas and power). See Note 6 for additional long-term debt provisions.

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****6. Long-Term Debt and Liquidity Matters**

All of Pinnacle West's and APS's debt is unsecured. The following table presents the components of long-term debt on the Consolidated Balance Sheets outstanding at December 31, 2018 and 2017 (dollars in thousands):

	Maturity Dates (a)	Interest Rates	December 31,	
			2018	2017
APS				
Pollution control bonds:				
Variable	2029	(b)	\$35,975	\$35,975
Fixed	2024	4.70%	115,150	147,150
Total pollution control bonds			151,125	183,125
Senior unsecured notes	2019-2048	2.20%-8.75%	4,575,000	4,275,000
Term loans		(c)	—	150,000
Unamortized discount			(12,638)	(11,288)
Unamortized premium			7,736	8,049
Unamortized debt issuance cost			(31,787)	(31,594)
Total APS long-term debt			4,689,436	4,573,292
Less current maturities			500,000	82,000
Total APS long-term debt less current maturities			4,189,436	4,491,292
Pinnacle West				
Senior unsecured notes	2020	2.25%	300,000	300,000
Term loan	2020	(d)	150,000	—
Unamortized discount			(121)	(184)
Unamortized debt issuance cost			(1,083)	(1,395)
Total Pinnacle West long-term debt			448,796	298,421
Less current maturities			—	—
Total Pinnacle West long-term debt less current maturities			448,796	298,421
TOTAL LONG-TERM DEBT LESS CURRENT MATURITIES			\$4,638,232	\$4,789,713

(a) This schedule does not reflect the timing of redemptions that may occur prior to maturities.

(b) The weighted-average rate for the variable rate pollution control bonds was 1.76% at December 31, 2018 and 1.77% at December 31, 2017.

(c) The weighted-average interest rate was 2.24% at December 31, 2017.

(d) The weighted-average interest rate was 3.02% at December 31, 2018.

The following table shows principal payments due on Pinnacle West's and APS's total long-term debt (dollars in thousands):

Year	Consolidated Pinnacle West	Consolidated APS
2019	\$500,000	\$500,000

2020	700,000	250,000
2021	—	—
2022	—	—
2023	—	—
Thereafter	3,976,125	3,976,125
Total	\$5,176,125	\$4,726,125

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Debt Fair Value**

Our long-term debt fair value estimates are classified within Level 2 of the fair value hierarchy. The following table represents the estimated fair value of our long-term debt, including current maturities (dollars in thousands):

	As of December 31, 2018		As of December 31, 2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Pinnacle West	\$448,796	\$443,955	\$298,421	\$298,608
APS	4,689,436	4,789,608	4,573,292	5,006,348
Total	\$5,138,232	\$5,233,563	\$4,871,713	\$5,304,956

Credit Facilities and Debt Issuances***Pinnacle West***

On December 21, 2018, Pinnacle West entered into a \$150 million term loan facility that matures December 2020. The proceeds were used for general corporate purposes.

APS

On May 30, 2018, APS purchased all \$32 million of Maricopa County, Arizona Pollution Control Corporation Pollution Control Revenue Refunding Bonds, 2009 Series C, due 2029. These bonds were classified as current maturities of long-term debt on our Consolidated Balance Sheets at December 31, 2017.

On June 26, 2018, APS repaid at maturity APS's \$50 million term loan facility.

On August 9, 2018, APS issued \$300 million of 4.20% unsecured senior notes that mature on August 15, 2048. The net proceeds from the sale of the notes were used to repay commercial paper borrowings.

On November 30, 2018, APS repaid its \$100 million term loan facility that would have matured April 22, 2019.

On December 21, 2018, Pinnacle West contributed \$150 million into APS in the form of an equity infusion. APS used this contribution to repay short-term indebtedness.

See “Lines of Credit and Short-Term Borrowings” in Note 5 and “Financial Assurances” in Note 10 for discussion of APS’s separate outstanding letters of credit.

Debt Provisions

Pinnacle West’s and APS’s debt covenants related to their respective bank financing arrangements include maximum debt to capitalization ratios. Pinnacle West and APS comply with this covenant. For both Pinnacle West and APS, this covenant requires that the ratio of consolidated debt to total consolidated capitalization not exceed 65%. At December 31, 2018, the ratio was approximately 50% for Pinnacle West and 46% for APS. 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.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Neither Pinnacle West's nor APS's 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 credit agreements contain a pricing grid in which the interest rates we pay for borrowings thereunder 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's 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 credit facility borrowings.

Although provisions in APS's articles of incorporation and ACC financing orders establish maximum amounts of preferred stock and debt that APS may issue, APS does not expect any of these provisions to limit its ability to meet its capital requirements. On November 27, 2018, the ACC issued a financing order in which, subject to specified parameters and procedures, it approved an increase in APS's long-term debt authorization from \$5.1 billion to \$5.9 billion in light of the projected growth of APS and its customer base and the resulting projected financing needs. See Note 5 for additional short-term debt provisions.

7. Retirement Plans and Other Postretirement Benefits

Pinnacle West sponsors a qualified defined benefit and account balance pension plan (The Pinnacle West Capital Corporation Retirement Plan) and a non-qualified supplemental excess benefit retirement plan for the employees of Pinnacle West and its subsidiaries. All new employees participate in the account balance plan. Defined benefit plans specify the amount of benefits a plan participant is to receive using information about the participant. The pension plan covers nearly all employees. The supplemental excess benefit retirement plan covers officers of the Company and highly compensated employees designated for participation by the Board of Directors. Our employees do not contribute to the plans. We calculate the benefits based on age, years of service and pay.

Pinnacle West also sponsors other postretirement benefit plans (Pinnacle West Capital Corporation Group Life and Medical Plan and Pinnacle West Capital Corporation Post-65

Retiree Health Reimbursement Arrangement) for the employees of Pinnacle West and its subsidiaries. These plans provide medical and life insurance benefits to retired employees. Employees must retire to become eligible for these retirement benefits, which are based on years of service and age. For the medical insurance plan, retirees make contributions to cover a portion of the plan costs. For the life insurance plan, retirees do not make contributions. We retain the right to change or eliminate these benefits.

Because of plan changes in 2014, the Company sought IRS approval to move approximately \$186 million of other postretirement benefit trust assets into a new trust account to pay for active union employee medical costs. In December 2016, FERC approved a methodology for determining the amount of other postretirement benefit trust assets to transfer into a new trust account to pay for active union employee medical costs. On January 2, 2018, these funds were moved to the new trust account, which is included in the other special use funds on the Consolidated Balance Sheets. The Company and the IRS executed a final Closing Agreement on March 2, 2018. The Company made an informational filing with FERC during February 2018. It is the Company's understanding that completion of these regulatory requirements permits access to approximately \$186 million for the sole purpose of paying active union employee medical benefits.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Pinnacle West uses a December 31 measurement date each year for its pension and other postretirement benefit plans. The market-related value of our plan assets is their fair value at the measurement date. See Note 13 for further discussion of how fair values are determined. Due to subjective and complex judgments, which may be required in determining fair values, actual results could differ from the results estimated through the application of these methods.

A significant portion of the changes in the actuarial gains and losses of our pension and postretirement plans is attributable to APS and therefore is recoverable in rates. Accordingly, these changes are recorded as a regulatory asset or regulatory liability.

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 thousands):

	Pension			Other Benefits		
	2018	2017	2016	2018	2017	2016
Service cost-benefits earned during the period	\$56,669	\$54,858	\$53,792	\$21,100	\$17,119	\$14,993
Interest cost on benefit obligation	124,689	129,756	131,647	28,147	29,959	29,721
Expected return on plan assets	(182,853)	(174,271)	(173,906)	(42,082)	(53,401)	(36,495)
Amortization of:						
Prior service cost (credit)	—	81	527	(37,842)	(37,842)	(37,883)
Net actuarial loss	32,082	47,900	40,717	—	5,118	4,589
Net periodic benefit cost (benefit)	\$30,587	\$58,324	\$52,777	\$(30,677)	\$(39,047)	\$(25,075)
Portion of cost charged to expense	\$10,120	\$27,295	\$26,172	\$(21,426)	\$(18,274)	\$(12,435)

On January 1, 2018, we adopted new accounting standard ASU 2017-07, Compensation-Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. This new standard changed our income statement presentation of net periodic benefit cost/(credits) and allows only the service cost component of net periodic benefit cost to be eligible for capitalization. See Note 2 for additional information.

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The following table shows the plans' changes in the benefit obligations and funded status for the years 2018 and 2017 (dollars in thousands):

	Pension		Other Benefits	
	2018	2017	2018	2017
Change in Benefit Obligation				
Benefit obligation at January 1	\$3,394,186	\$3,204,462	\$753,393	\$716,445
Service cost	56,669	54,858	21,100	17,119
Interest cost	124,689	129,756	28,147	29,959
Benefit payments	(184,161)	(166,342)	(31,540)	(30,144)
Actuarial (gain) loss	(200,757)	171,452	(94,329)	20,014
Benefit obligation at December 31	3,190,626	3,394,186	676,771	753,393
Change in Plan Assets				
Fair value of plan assets at January 1	3,057,027	2,675,357	1,022,371	882,651
Actual return on plan assets	(201,078)	428,374	(40,354)	139,367
Employer contributions	50,000	100,000	—	353
Benefit payments	(172,473)	(146,704)	(72,453)	—
Transfer to active union medical account	—	—	(185,887)	—
Fair value of plan assets at December 31	2,733,476	3,057,027	723,677	1,022,371
Funded Status at December 31	\$(457,150)	\$(337,159)	\$46,906	\$268,978

The following table shows the projected benefit obligation and the accumulated benefit obligation for pension plans with an accumulated obligation in excess of plan assets as of December 31, 2018 and 2017 (dollars in thousands):

	2018	2017
Projected benefit obligation	\$3,190,626	\$3,394,186
Accumulated benefit obligation	3,038,774	3,227,233
Fair value of plan assets	2,733,476	3,057,027

The following table shows the amounts recognized on the Consolidated Balance Sheets as of December 31, 2018 and 2017 (dollars in thousands):

	Pension		Other Benefits	
	2018	2017	2018	2017
Noncurrent asset	\$—	\$—	\$46,906	\$268,978
Current liability	(13,980)	(9,859)	—	—
Noncurrent liability	(443,170)	(327,300)	—	—
Net amount recognized	\$(457,150)	\$(337,159)	\$46,906	\$268,978

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The following table shows the details related to accumulated other comprehensive loss as of December 31, 2018 and 2017 (dollars in thousands):

	Pension		Other Benefits	
	2018	2017	2018	2017
Net actuarial loss	\$794,292	\$643,199	\$63,544	\$75,439
Prior service credit	—	—	(227,733)	(265,575)
APS's portion recorded as a regulatory (asset) liability	(733,351)	(576,188)	163,767	189,627
Income tax expense (benefit)	(15,083)	(24,915)	561	853
Accumulated other comprehensive loss	\$45,858	\$42,096	\$139	\$344

The following table shows the estimated amounts that will be amortized from accumulated other comprehensive loss and regulatory assets and liabilities into net periodic benefit cost in 2019 (dollars in thousands):

	Pension	Other Benefits
Net actuarial loss	\$43,248	\$—
Prior service credit	—	(37,821)
Total amounts estimated to be amortized from accumulated other comprehensive loss (gain) and regulatory assets (liabilities) in 2019	\$43,248	\$(37,821)

The following table shows the weighted-average assumptions used for both the pension and other benefits to determine benefit obligations and net periodic benefit costs:

	Benefit Obligations		Benefit Costs		
	As of December 31,		For the Years Ended December 31,		
	2018	2017	2018	2017	2016
Discount rate – pension	4.34 %	3.65 %	3.65 %	4.08 %	4.37 %
Discount rate – other benefits	4.39 %	3.71 %	3.71 %	4.17 %	4.52 %
Rate of compensation increase	4.00 %	4.00 %	4.00 %	4.00 %	4.00 %
Expected long-term return on plan assets - pension	N/A	N/A	6.05 %	6.55 %	6.90 %
Expected long-term return on plan assets - other benefits	N/A	N/A	5.40 %	6.05 %	4.45 %
Initial healthcare cost trend rate (pre-65 participants)	7.00 %	7.00 %	7.00 %	7.00 %	7.00 %
Initial healthcare cost trend rate (post-65 participants)	4.75 %	4.75 %	4.75 %	5.00 %	5.00 %
Ultimate healthcare cost trend rate	4.75 %	4.75 %	4.75 %	5.00 %	5.00 %
Number of years to ultimate trend rate (pre-65 participants)	7	8	8	4	4

In selecting the pretax expected long-term rate of return on plan assets, we consider past performance and economic forecasts for the types of investments held by the plan. For 2019, we are assuming a 6.25% long-term rate of return for pension assets and 5.55% (before tax) for other benefit assets, which we believe is reasonable given our asset allocation in relation

to historical and expected performance.

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In selecting our healthcare trend rates, we consider past performance and forecasts of healthcare costs. A one percentage point change in the assumed initial and ultimate healthcare cost trend rates would have the following effects on our December 31, 2018 amounts (dollars in thousands):

	1% Increase	1% Decrease
Effect on other postretirement benefits expense, after consideration of amounts capitalized or billed to electric plant participants	\$ 10,235	\$(4,322)
Effect on service and interest cost components of net periodic other postretirement benefit costs	11,223	(8,479)
Effect on the accumulated other postretirement benefit obligation	101,224	(81,144)

Plan Assets

The Board of Directors has delegated oversight of the pension and other postretirement benefit plans' assets to an Investment Management Committee ("Committee"). The Committee has adopted investment policy statements ("IPS") for the pension and the other postretirement benefit plans' assets. The investment strategies for these plans include external management of plan assets, and prohibition of investments in Pinnacle West securities.

The overall strategy of the pension plan's IPS is to achieve an adequate level of trust assets relative to the benefit obligations. To achieve this objective, the plan's investment policy provides for mixes of investments including long-term fixed income assets and return-generating assets. The target allocation between return-generating and long-term fixed income assets is defined in the IPS and is a function of the plan's funded status. The plan's funded status is reviewed on at least a monthly basis.

Changes in the value of long-term fixed income assets, also known as liability-hedging assets, are intended to offset changes in the benefit obligations due to changes in interest rates. Long-term fixed income assets consist primarily of fixed income debt securities issued by the U.S. Treasury and other government agencies, U.S. Treasury Futures Contracts, and fixed income debt securities issued by corporations. Long-term fixed income assets may also include interest rate swaps, and other instruments.

Return-generating assets are intended to provide a reasonable long-term rate of investment return with a prudent level of volatility. Return-generating assets are composed of U.S. equities, international equities, and alternative investments. International equities include investments in both developed and emerging markets. Alternative investments include

investments in real estate, private equity and various other strategies. The plan may also hold investments in return-generating assets by holding securities in partnerships, common and collective trusts and mutual funds.

Based on the IPS, and given the pension plan's funded status at year-end 2018, the target and actual allocation for the pension plan at December 31, 2018 are as follows:

	Pension			
	Target	Actual	Target	Actual
	Allocation	Allocation	Allocation	Allocation
Long-term fixed income assets	62 %	64 %		
Return-generating assets	38 %	36 %		
Total	100 %	100 %		

The permissible range is within +/- 3% of the target allocation shown in the above table, and also considers the Plan's funded status.

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The following table presents the additional target allocations, as a percent of total pension plan assets, for the return-generating assets:

Asset Class	Target Allocation	
Equities in US and other developed markets	18	%
Equities in emerging markets	6	%
Alternative investments	14	%
Total	38	%

The pension plan IPS does not provide for a specific mix of long-term fixed income assets, but does expect the average credit quality of such assets to be investment grade.

As of December 31, 2018, the asset allocation for other postretirement benefit plan assets is governed by the IPS for those plans, which provides for different asset allocation target mixes depending on the characteristics of the liability. Some of these asset allocation target mixes vary with the plan's funded status. The following table presents the actual allocations of the investment for the other postretirement benefit plan at December 31, 2018:

	Other Benefits Actual Allocation	
Long-term fixed income assets	69	%
Return-generating assets	31	%
Total	100	%

See Note 13 for a discussion on the fair value hierarchy and how fair value methodologies are applied. The plans invest directly in fixed income, U.S. Treasury Futures Contracts, and equity securities, in addition to investing indirectly in fixed income securities, equity securities and real estate through the use of mutual funds, partnerships and common and collective trusts. Equity securities held directly by the plans are valued using quoted active market prices from the published exchange on which the equity security trades, and are classified as Level 1. U.S. Treasury Futures Contracts are valued using the quoted active market prices from the exchange on which they trade, and are classified as Level 1. Fixed income securities issued by the U.S. Treasury held directly by the plans are valued using quoted active market prices, and are classified as Level 1. Fixed income securities issued by

corporations, municipalities, and other agencies are primarily valued using quoted inactive market prices, or quoted active market prices for similar securities, or by utilizing calculations which incorporate observable inputs such as yield, maturity and credit quality. These instruments are classified as Level 2.

Mutual funds, partnerships, and common and collective trusts are valued utilizing a net asset value (NAV) concept or its equivalent. Mutual funds, which includes exchange traded funds (ETFs), are classified as Level 1 and valued using a NAV that is observable and based on the active market in which the fund trades.

Common and collective trusts are maintained by banks or investment companies and hold certain investments in accordance with a stated set of objectives (such as tracking the performance of the S&P 500 Index). The trust's shares are offered to a limited group of investors, and are not traded in an active market. Investments in common and collective trusts are valued using NAV as a practical expedient and, accordingly, are not classified in the fair value hierarchy. The NAV for trusts investing in exchange traded equities, and fixed income securities is derived from the market prices of the underlying securities held by the trusts. The

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NAV for trusts investing in real estate is derived from the appraised values of the trust's underlying real estate assets. As of December 31, 2018, the plans were able to transact in the common and collective trusts at NAV.

Investments in partnerships are also valued using the concept of NAV as a practical expedient and, accordingly, are not classified in the fair value hierarchy. The NAV for these investments is derived from the value of the partnerships' underlying assets. The plan's partnerships holdings relate to investments in high-yield fixed income instruments and assets of privately held portfolio companies. Certain partnerships also include funding commitments that may require the plan to contribute up to \$75 million to these partnerships; as of December 31, 2018, approximately \$62 million of these commitments have been funded.

The plans' trustee provides valuation of our plan assets by using pricing services that utilize methodologies described to determine fair market value. We have internal control procedures to ensure this information is consistent with fair value accounting guidance. These procedures include assessing valuations using an independent pricing source, verifying that pricing can be supported by actual recent market transactions, assessing hierarchy classifications, comparing investment returns with benchmarks, and obtaining and reviewing independent audit reports on the trustee's internal operating controls and valuation processes.

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The fair value of Pinnacle West's pension plan and other postretirement benefit plan assets at December 31, 2018, by asset category, are as follows (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Other (a)	Balance at December 31, 2018
Pension Plan:				
Cash and cash equivalents	\$ 451	\$—	\$—	\$451
Fixed income securities:				
Corporate	—	1,237,744	—	1,237,744
U.S. Treasury	372,649	—	—	372,649
Other (b)	—	78,902	—	78,902
Common stock equities (c)	196,661	—	—	196,661
Mutual funds (d)	120,976	—	—	120,976
Common and collective trusts:				
Equities	—	—	272,926	272,926
Real estate	—	—	165,123	165,123
Fixed Income	—	—	86,483	86,483
Partnerships	—	—	125,217	125,217
Short-term investments and other (e)	—	—	76,344	76,344
Total	\$ 690,737	\$ 1,316,646	\$ 726,093	\$ 2,733,476
Other Benefits:				
Cash and cash equivalents	\$ 93	\$—	\$—	\$93
Fixed income securities:				
Corporate	—	163,286	—	163,286
U.S. Treasury	318,017	—	—	318,017
Other (b)	—	7,531	—	7,531
Common stock equities (c)	129,199	—	—	129,199
Mutual funds (d)	10,963	—	—	10,963
Common and collective trusts:				
Equities	—	—	65,720	65,720
Real estate	—	—	19,054	19,054
Short-term investments and other (e)	3,633	—	6,181	9,814
Total	\$ 461,905	\$ 170,817	\$ 90,955	\$ 723,677

(a) These investments primarily represent assets valued using net asset value as a practical expedient, and have not been classified in the fair value hierarchy.

(b) This category consists primarily of debt securities issued by municipalities.

(c) This category primarily consists of U.S. common stock equities.

(d) These funds invest in international common stock equities.

(e) This category includes plan receivables and payables.

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The fair value of Pinnacle West's pension plan and other postretirement benefit plan assets at December 31, 2017, by asset category, are as follows (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Other (a)	Balance at December 31, 2017
Pension Plan:				
Cash and cash equivalents	\$ 3,830	\$—	\$—	\$3,830
Fixed income securities:				
Corporate	—	1,365,194	—	1,365,194
U.S. Treasury	221,291	—	—	221,291
Other (b)	—	100,599	—	100,599
Common stock equities (c)	228,088	—	—	228,088
Mutual funds (d)	233,732	—	—	233,732
Common and collective trusts:				
Equities	—	—	408,763	408,763
Real estate	—	—	171,569	171,569
Fixed Income	—	—	90,869	90,869
Partnerships	—	—	133,379	133,379
Short-term investments and other (e)	—	1,208	98,505	99,713
Total	\$ 686,941	\$ 1,467,001	\$ 903,085	\$ 3,057,027
Other Benefits:				
Cash and cash equivalents	\$ 143	\$—	\$—	\$ 143
Fixed income securities:				
Corporate	—	306,008	—	306,008
U.S. Treasury	336,963	—	—	336,963
Other (b)	—	32,508	—	32,508
Common stock equities (c)	196,153	—	—	196,153
Mutual funds (d)	39,269	—	—	39,269
Common and collective trusts:				
Equities	—	—	75,310	75,310
Real estate	—	—	15,422	15,422
Short-term investments and other (e)	11,268	149	9,178	20,595
Total	\$ 583,796	\$ 338,665	\$ 99,910	\$ 1,022,371

(a) These investments primarily represent assets valued using net asset value as a practical expedient, and have not been classified in the fair value hierarchy.

(b) This category consists primarily of debt securities issued by municipalities.

(c) This category primarily consists of U.S. common stock equities.

(d) These funds invest in U.S. and international common stock equities.

(e) This category includes plan receivables and payables.

Contributions

Future year contribution amounts are dependent on plan asset performance and plan actuarial assumptions. We made contributions to our pension plan totaling \$50 million in 2018, \$100 million in 2017, and \$100 million in 2016. The minimum required contributions for the pension plan are zero for the next three years. We expect to make voluntary contributions up to a total of \$350 million during the 2019-2021 period.

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With regard to contributions to our other postretirement benefit plan, we did not make a contribution in 2018. We made a contribution of approximately \$1 million in each of 2017 and 2016. We do not expect to make any contributions over the next three years to our other postretirement benefit plans. In 2018, the Company was reimbursed \$72 million for prior years retiree medical claims from the other postretirement benefit plan trust assets.

Estimated Future Benefit Payments

Benefit payments, which reflect estimated future employee service, for the next five years and the succeeding five years thereafter, are estimated to be as follows (dollars in thousands):

Year	Pension	Other Benefits
2019	\$ 188,492	\$ 32,622
2020	193,087	34,199
2021	198,471	35,551
2022	204,399	36,673
2023	211,346	37,405
Years 2024-2028	1,093,319	187,023

Electric plant participants contribute to the above amounts in accordance with their respective participation agreements.

Employee Savings Plan Benefits

Pinnacle West sponsors a defined contribution savings plan for eligible employees of Pinnacle West and its subsidiaries. In 2018, costs related to APS's employees represented 99% of the total cost of this plan. In a defined contribution savings plan, the benefits a participant receives result from regular contributions participants make to their own individual account, the Company's matching contributions and earnings or losses on their investments. Under this plan, the Company matches a percentage of the participants' contributions in cash which is then invested in the same investment mix as participants elect to invest their own future contributions. Pinnacle West recorded expenses for this plan of approximately \$11 million for 2018, \$10 million for 2017, and \$10 million for 2016.

8. Leases

We lease certain vehicles, land, buildings, equipment and miscellaneous other items through operating rental agreements with varying terms, provisions and expiration dates.

Lease expense recognized in the Consolidated Statements of Income was \$18 million in 2018, \$18 million in 2017, and \$16 million in 2016. APS's lease expense was \$17 million in 2018, \$17 million in 2017, and \$15 million in 2016. These amounts do not include purchased power lease contracts, discussed below.

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Estimated future minimum lease payments for Pinnacle West's and APS's operating leases, excluding purchased power agreements, are approximately as follows (dollars in thousands):

Year	Pinnacle West Consolidated	APS
2019	\$ 13,747	\$13,411
2020	12,428	12,143
2021	9,478	9,282
2022	6,513	6,321
2023	5,359	5,171
Thereafter	42,236	40,656
Total future lease commitments	\$ 89,761	\$86,984

In 1986, APS entered into agreements with three separate lessor trust entities in order to sell and lease back interests in Palo Verde Unit 2 and related common facilities. These lessor trust entities have been deemed VIEs for which APS is the primary beneficiary. As the primary beneficiary, APS consolidated these lessor trust entities. The impacts of these sale leaseback transactions are excluded from our lease disclosures as lease accounting is eliminated upon consolidation. See Note 18 for a discussion of VIEs.

Purchased Power Lease Contracts

A purchased power contract may contain a lease for accounting purposes. This generally occurs when a purchased power contract designates a specific power plant from which the buyer purchases substantially all of the output and also meets other required lease accounting criteria. APS has certain purchased power contracts that contain lease arrangements. The future minimum lease payments due under these contracts are \$54 million, all of which relate to 2019. Due to the inherent uncertainty associated with the reliability of the fuel source, payments under most renewable purchased power lease contracts are considered contingent rents and are excluded from future minimum lease payments. See Note 10 for additional information on our purchased power contract estimated commitments.

Operating lease cost for purchased power lease contracts was \$47 million in 2018, \$60 million in 2017 and \$82 million in 2016. In addition, contingent rents for purchased power lease contracts was \$109 million in 2018, \$100 million in 2017, and \$88 million in 2016. These costs are recorded in fuel and purchased power on the Consolidated Statements of Income, and are subject to recovery under the PSA or RES. See Note 3.

See Note 2 for a discussion of the new lease accounting standard we adopted on January 1, 2019.

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APS shares ownership of some of its generating and transmission facilities with other companies. We are responsible for our share of operating costs which are included in the corresponding operating expenses on our Consolidated Statements of Income. We are also responsible for providing our own financing. Our share of operating expenses and utility plant costs related to these facilities is accounted for using proportional consolidation. The following table shows APS's interests in those jointly-owned facilities recorded on the Consolidated Balance Sheets at December 31, 2018 (dollars in thousands):

	Percent Owned	Plant in Service	Accumulated Depreciation	Construction Work in Progress
Generating facilities:				
Palo Verde Units 1 and 3	29.1%	\$1,887,729	\$1,095,878	\$ 25,185
Palo Verde Unit 2 (a)	16.8%	638,419	369,372	20,852
Palo Verde Common	28.0% (b)	752,300	277,414	39,995
Palo Verde Sale Leaseback	(a)	351,050	245,275	—
Four Corners Generating Station	63.0%	1,466,579	544,308	23,430
Cholla common facilities (c)	50.5%	183,390	82,434	893
Transmission facilities:				
ANPP 500kV System	33.5% (b)	129,587	49,340	2,705
Navajo Southern System	26.7% (b)	82,046	30,464	284
Palo Verde — Yuma 500kV System	19.0% (b)	15,304	6,729	530
Four Corners Switchyards	63.1% (b)	68,707	15,436	1,334
Phoenix — Mead System	17.1% (b)	39,329	18,527	44
Palo Verde — Rudd 500kV System	50.0%	93,887	25,573	302
Morgan — Pinnacle Peak System	64.6% (b)	117,722	16,744	—
Round Valley System	50.0%	515	153	—
Palo Verde — Morgan System	87.9% (b)	219,292	6,660	—
Hassayampa — North Gila System	80.0%	142,541	9,805	—
Cholla 500kV Switchyard	85.7%	5,078	1,414	38
Saguaro 500kV Switchyard	60.0%	20,414	12,790	—
Kyrene — Knox System	50.0%	578	307	—

(a) See Note 18.

(b) Weighted-average of interests.

(c) PacifiCorp owns Cholla Unit 4 and APS operates the unit for PacifiCorp. The common facilities at Cholla are jointly-owned.

APS also has a 14% ownership in the Navajo Plant. In the second quarter of 2017, APS's remaining net book value of its interest was reclassified from property, plant and equipment to a regulatory asset. See "Navajo Plant" in Note 3 for more details.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**10. Commitments and Contingencies****Palo Verde Generating Station****Spent Nuclear Fuel and Waste Disposal**

On December 19, 2012, APS, acting on behalf of itself and the participant owners of Palo Verde, filed a second breach of contract lawsuit against the DOE in the United States Court of Federal Claims ("Court of Federal Claims"). The lawsuit sought to recover damages incurred due to the DOE's breach of the Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste ("Standard Contract") for failing to accept Palo Verde's spent nuclear fuel and high level waste from January 1, 2007 through June 30, 2011, as it was required to do pursuant to the terms of the Standard Contract and the Nuclear Waste Policy Act. On August 18, 2014, APS and the DOE entered into a settlement agreement, stipulating to a dismissal of the lawsuit and payment of \$57.4 million by the DOE to the Palo Verde owners for certain specified costs incurred by Palo Verde during the period January 1, 2007 through June 30, 2011. APS's share of this amount is \$16.7 million. Amounts recovered in the lawsuit and settlement were recorded as adjustments to a regulatory liability and had no impact on the amount of reported net income. In addition, the settlement agreement, as amended, provides APS with a method for submitting claims and getting recovery for costs incurred through December 31, 2019.

APS has submitted four claims pursuant to the terms of the August 18, 2014 settlement agreement, for four separate time periods during July 1, 2011 through June 30, 2018. The DOE has approved and paid \$74.2 million for these claims (APS's share is \$21.6 million). The amounts recovered were primarily recorded as adjustments to a regulatory liability and had no impact on reported net income. In accordance with the 2017 Rate Case Decision, this regulatory liability is being refunded to customers (see Note 3). APS's next claim pursuant to the terms of the August 18, 2014 settlement agreement was submitted to the DOE on October 31, 2018 in the amount of \$10.2 million (APS's share is \$3.0 million). This claim is pending DOE review.

Nuclear Insurance

Public liability for incidents at nuclear power plants is governed by the Price-Anderson Nuclear Industries Indemnity Act ("Price-Anderson Act"), which limits the liability of

nuclear reactor owners to the amount of insurance available from both commercial sources and an industry-wide retrospective payment plan. In accordance with the Price-Anderson Act, the Palo Verde participants are insured against public liability for a nuclear incident of up to approximately \$14.1 billion per occurrence. Palo Verde maintains the maximum available nuclear liability insurance in the amount of \$450 million, which is provided by American Nuclear Insurers ("ANI"). The remaining balance of approximately \$13.6 billion of liability coverage is provided through a mandatory industry-wide retrospective premium program. If losses at any nuclear power plant covered by the program exceed the accumulated funds, APS could be responsible for retrospective premiums. The maximum retrospective premium per reactor under the program for each nuclear liability incident is approximately \$137.6 million, subject to a maximum annual premium of approximately \$20.5 million per incident. Based on APS's ownership interest in the three Palo Verde units, APS's maximum retrospective premium per incident for all three units is approximately \$120.1 million, with a maximum annual retrospective premium of approximately \$17.9 million.

The Palo Verde participants maintain insurance for property damage to, and decontamination of, property at Palo Verde in the aggregate amount of \$2.8 billion. APS has also secured accidental outage insurance for a sudden and unforeseen accidental outage of any of the three units. The property damage, decontamination, and accidental outage insurance are provided by Nuclear Electric Insurance Limited

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("NEIL"). APS is subject to retrospective premium adjustments 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 \$24.8 million for each retrospective premium 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 \$71.2 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, sublimits and exclusions.

Fuel and Purchased Power Commitments and Purchase Obligations

APS is party to various fuel and purchased power contracts and purchase obligations with terms expiring between 2019 and 2043 that include required purchase provisions. APS estimates the contract requirements to be approximately \$622 million in 2019; \$555 million in 2020; \$558 million in 2021; \$563 million in 2022; \$560 million in 2023; and \$5.9 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 include estimated commitments relating to purchased power lease contracts, see Note 8.

Of the various fuel and purchased power contracts mentioned above, some of those contracts for coal supply include take-or-pay provisions. The current coal contracts with take-or-pay provisions have terms expiring through 2031.

The following table summarizes our estimated coal take-or-pay commitments (dollars in thousands):

	Years Ended December 31,					
	2019	2020	2021	2022	2023	Thereafter
Coal take-or-pay commitments (a)	\$179,879	\$181,059	\$184,944	\$186,244	\$187,518	\$1,422,253

(a) Total take-or-pay commitments are approximately \$2.3 billion. The total net present value of these commitments is approximately \$1.7 billion.

APS may spend more to meet its actual fuel requirements than the minimum purchase obligations in our coal take-or-pay contracts. The following table summarizes actual amounts purchased under the coal contracts which include take-or-pay provisions for each of

the last three years (dollars in thousands):

	Year Ended December 31,		
	2018	2017	2016
Total purchases	\$206,093	\$165,220	\$160,066

Renewable Energy Credits

APS has entered into contracts to purchase renewable energy credits to comply with the RES. APS estimates the contract requirements to be approximately \$37 million in 2019; \$36 million in 2020; \$34 million in 2021; \$31 million in 2022; \$30 million in 2023; and \$155 million thereafter. These amounts do not include purchases of renewable energy credits that are bundled with energy.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Coal Mine Reclamation Obligations

APS must reimburse certain coal providers for amounts incurred for final and contemporaneous coal mine reclamation. We account for contemporaneous reclamation costs as part of the cost of the delivered coal. We utilize site-specific studies of costs expected to be incurred in the future to estimate our final reclamation obligation. These studies utilize various assumptions to estimate the future costs. Based on the most recent reclamation studies, APS recorded an obligation for the coal mine final reclamation of approximately \$213 million at December 31, 2018 and \$216 million at December 31, 2017. Under our current coal supply agreements, APS expects to make payments for the final mine reclamation as follows: \$32 million in 2019; \$21 million in 2020; \$21 million in 2021; \$22 million in 2022; \$24 million in 2023; and \$167 million thereafter. Any amendments to current coal supply agreements may change the timing of the contribution. Portions of these funds will be held in an escrow account and distributed to certain coal providers under the terms of the applicable coal supply agreements.

Superfund-Related Matters

The Comprehensive Environmental Response Compensation and Liability Act ("CERCLA" or "Superfund") establishes liability for the cleanup of hazardous substances found contaminating the soil, water or air. Those who released, generated, transported to, or disposed of hazardous substances at a contaminated site are among the parties who are potentially responsible ("PRPs"). PRPs may be strictly, and often are jointly and severally, liable for clean-up. On September 3, 2003, EPA advised APS that 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 EPA to perform certain investigative activities of the APS facilities within OU3. In addition, on September 23, 2009, APS agreed with EPA and one other PRP to voluntarily assist with the funding and management of the site-wide groundwater remedial investigation and feasibility study ("RI/FS"). Based upon discussions between the OU3 working group parties and EPA, along with the results of recent technical analyses prepared by the OU3 working group to supplement the RI/FS for OU3, APS anticipates finalizing the RI/FS in the fall or winter of 2019. We estimate that our costs related to this investigation and study will be approximately \$2 million. 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 expenditures related to this matter cannot be

reasonably estimated.

On August 6, 2013, Roosevelt Irrigation District ("RID") filed a lawsuit in Arizona District Court against APS and 24 other defendants, alleging that RID's groundwater wells were contaminated by the release of hazardous substances from facilities owned or operated by the defendants. The lawsuit also alleges that, under Superfund laws, the defendants are jointly and severally liable to RID. The allegations against APS arise out of APS's current and former ownership of facilities in and around OU3. As part of a state governmental investigation into groundwater contamination in this area, on January 25, 2015, ADEQ sent a letter to APS seeking information concerning the degree to which, if any, APS's current and former ownership of these facilities may have contributed to groundwater contamination in this area. APS responded to ADEQ on May 4, 2015. On December 16, 2016, two RID environmental and engineering contractors filed an ancillary lawsuit for recovery of costs against APS and the other defendants in the RID litigation. That same day, another RID service provider filed an additional ancillary CERCLA lawsuit against certain of the defendants in the main RID litigation, but excluded APS and certain other parties as named defendants. Because the ancillary lawsuits concern past costs allegedly incurred by these RID vendors, which were ruled unrecoverable directly by RID in November of 2016, the additional lawsuits do not increase APS's exposure or risk related to these matters.

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On April 5, 2018, RID and the defendants in that particular litigation executed a settlement agreement, fully resolving RID's CERCLA claims concerning both past and future cost recovery. APS's share of this settlement was immaterial. In addition, the two environmental and engineering vendors voluntarily dismissed their lawsuit against APS and the other named defendants without prejudice. An order to this effect was entered on April 17, 2018. With this disposition of the case, the vendors may file their lawsuit again in the future. In addition, APS and certain other parties not named in the remaining RID service provider lawsuit may be brought into the litigation via third-party complaints filed by the current direct defendants. We are unable to predict the outcome of these matters; however, we do not expect the outcome to have a material impact on our financial position, results of operations or cash flows.

Environmental Matters

APS is subject to numerous environmental laws and regulations affecting many aspects of its present and future operations, including air emissions of both conventional pollutants and greenhouse gases, water quality, wastewater discharges, solid waste, hazardous waste, and CCRs. These laws and regulations can change from time to time, imposing new obligations on APS resulting in increased capital, operating, and other costs. Associated capital expenditures or operating costs could be material. APS intends to seek recovery of any such environmental compliance costs through our rates, but cannot predict whether it will obtain such recovery. The following proposed and final rules involve material compliance costs to APS.

Regional Haze Rules. APS has received the final rulemaking imposing new pollution control requirements on Four Corners and the Navajo Plant. EPA will require these plants to install pollution control equipment that constitutes BART to lessen the impacts of emissions on visibility surrounding the plants. In addition, EPA issued a final rule for Regional Haze compliance at Cholla that does not involve the installation of new pollution controls and that will replace an earlier BART determination for this facility. See below for details of the Cholla BART approval.

Four Corners. Based on EPA's final standards, APS's 63% share of the cost of required controls for Four Corners Units 4 and 5 is approximately \$400 million, the majority of which has already been incurred. In addition, APS and El Paso entered into an asset purchase agreement providing for the purchase by APS, or an affiliate of APS, of El Paso's 7% interest

in Four Corners Units 4 and 5. 4CA purchased the El Paso interest on July 6, 2016. NTEC purchased the interest from 4CA on July 3, 2018. See "Four Corners Coal Supply Agreement - 4CA Matter" below for a discussion of the NTEC purchase. The cost of the pollution controls related to the 7% interest is approximately \$45 million, which was assumed by NTEC through its purchase of the 7% interest.

Navajo Plant. APS estimates that its share of costs for upgrades at the Navajo Plant, based on EPA's Federal Implementation Plan ("FIP"), could be up to approximately \$200 million; however, given the future plans for the Navajo Plant, we do not expect to incur these costs. See "Navajo Plant" in Note 3 for information regarding future plans for the Navajo Plant.

Cholla. APS believed that EPA's original 2012 final rule establishing controls constituting BART for Cholla, which would require installation of SCR controls, was unsupported and that EPA had no basis for disapproving Arizona's State Implementation Plan ("SIP") and promulgating a FIP that was inconsistent with the state's considered BART determinations under the regional haze program. In September 2014, APS met with EPA to propose a compromise BART strategy, whereby APS would permanently close Cholla Unit 2 and cease burning coal at Units 1 and 3 by the mid-2020s. (See Note 3 for details related to the resulting regulatory asset.) APS made the proposal with the understanding that additional emission control equipment is unlikely to be required in the future because retiring and/or converting the units as contemplated in the proposal is more

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cost effective than, and will result in increased visibility improvement over, the BART requirements for oxides of nitrogen ("NOx") imposed through EPA's BART FIP. In early 2017, EPA approved a final rule incorporating APS's compromise proposal, which took effect for Cholla on April 26, 2017.

Coal Combustion Waste. On December 19, 2014, EPA issued its final regulations governing the handling and disposal of CCR, such as fly ash and bottom ash. The rule regulates CCR as a non-hazardous waste under Subtitle D of the Resource Conservation and Recovery Act ("RCRA") and establishes national minimum criteria for existing and new CCR landfills and surface impoundments and all lateral expansions consisting of location restrictions, design and operating criteria, groundwater monitoring and corrective action, closure requirements and post closure care, and recordkeeping, notification, and internet posting requirements. The rule generally requires any existing unlined CCR surface impoundment that is contaminating groundwater above a regulated constituent's groundwater protection standard to stop receiving CCR and either retrofit or close, and further requires the closure of any CCR landfill or surface impoundment that cannot meet the applicable performance criteria for location restrictions or structural integrity. Such closure requirements are deemed "forced closure" or "closure for cause" of unlined surface impoundments, and are the subject of recent regulatory and judicial activities described below.

On December 16, 2016, President Obama signed the Water Infrastructure Improvements for the Nation ("WIIN") Act into law, which contains a number of provisions requiring EPA to modify the self-implementing provisions of the Agency's current CCR rules under Subtitle D. Such modifications include new EPA authority to directly enforce the CCR rules through the use of administrative orders and providing states, like Arizona, where the Cholla facility is located, the option of developing CCR disposal unit permitting programs, subject to EPA approval. For facilities in states that do not develop state-specific permitting programs, EPA is required to develop a federal permit program, pending the availability of congressional appropriations. By contrast, for facilities located within the boundaries of Native American tribal reservations, such as the Navajo Nation, where the Navajo Plant and Four Corners facilities are located, EPA is required to develop a federal permit program regardless of appropriated funds.

ADEQ has initiated a process to evaluate how to develop a state CCR permitting program that would cover electric generating units ("EGUs"), including Cholla. While APS has been working with ADEQ on the development of this program, we are unable to predict when

Arizona will be able to finalize and secure EPA approval for a state-specific CCR permitting program. With respect to the Navajo Nation, APS has sought clarification as to when and how EPA would be initiating permit proceedings for facilities on the reservation, including Four Corners. We are unable to predict at this time when EPA will be issuing CCR management permits for the facilities on the Navajo Nation. At this time, it remains unclear how the CCR provisions of the WIIN Act will affect APS and its management of CCR.

Based upon utility industry petitions for EPA to reconsider the RCRA Subtitle D regulations for CCR, which were premised in part on the CCR provisions of the 2016 WIIN Act, on September 13, 2017 EPA agreed to evaluate whether to revise these federal CCR regulations. On July 17, 2018, EPA finalized a revision to its RCRA Subtitle D regulations for CCR, the "Phase I, Part I" revision to its CCR regulations, deferring for future action a number of other proposed changes contemplated in a March 1, 2018 proposal. For the final rule issued on July 17, 2018, EPA established nationwide health-based standards for certain constituents of CCR subject to groundwater corrective action and delayed the closure deadlines for certain unlined CCR surface impoundments by 18 months (for example, those disposal units required to undergo forced closure). These changes to the federal regulations governing CCR disposal are unlikely to have a material impact on APS. As for those aspects of the March 2018 rulemaking proposal for which EPA has yet to take final action, it remains unclear which specific provisions of the federal CCR rules will ultimately be modified, how they will be modified, or when such modification will occur.

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Pursuant to a June 24, 2016 order by the D.C. Circuit Court of Appeals in the litigation by industry- and environmental-groups challenging EPA's CCR regulations, EPA is required to complete a rulemaking proceeding in the near future concerning whether or not boron must be included on the list of groundwater constituents that might trigger corrective action under EPA's CCR rules. Simultaneously with the issuance of EPA's proposed modifications to the federal CCR rules in response to industry petitions, on March 1, 2018, EPA issued a proposed rule seeking comment as to whether or not boron should be included on this list. EPA is not required to take final action approving the inclusion of boron. Should EPA take final action adding boron to the list of groundwater constituents that might trigger corrective action, any resulting corrective action measures may increase APS's costs of compliance with the CCR rule at our coal-fired generating facilities. At this time APS cannot predict the eventual results of this rulemaking proceeding concerning boron.

On August 21, 2018, the D.C. Circuit Court issued its decision on the merits in this litigation. The Court upheld the legality of EPA's CCR regulations, though it vacated and remanded back to EPA a number of specific provisions, which are to be corrected in accordance with the Court's order. Among the issues affecting APS's management of CCR, the D.C. Circuit's decision vacated and remanded those provisions of the EPA CCR regulations that allow for the operation of unlined CCR surface impoundments, even where those unlined impoundments have not otherwise violated a regulatory location restriction or groundwater protection standard (i.e., otherwise triggering forced closure). At this time, it remains unclear how this D.C. Circuit Court decision will affect APS's operations or any financial impacts, as EPA has yet to take regulatory action on remand to revise its 2015 CCR regulations consistent with the Court's order.

Based on this decision, on December 17, 2018, certain environmental groups filed an emergency motion with the D.C. Circuit to either stay or summarily vacate EPA's July 17, 2018 final rule extending the closure-initiation deadline for certain unlined CCR surface impoundments until October 2020. In response, EPA filed a motion to remand but not vacate that deadline extension regulation. We cannot predict the outcome of the D.C. Circuit's consideration of these dueling motions, and whether or how such a ruling would affect APS's operations.

APS currently disposes of CCR in ash ponds and dry storage areas at Cholla and Four Corners. APS estimates that its share of incremental costs to comply with the CCR rule for Four Corners is approximately \$22 million and its share of incremental costs to comply with

the CCR rule for Cholla is approximately \$20 million. The Navajo Plant currently disposes of CCR in a dry landfill storage area. APS estimates that its share of incremental costs to comply with the CCR rule for the Navajo Plant is approximately \$1 million. Additionally, the CCR rule requires ongoing, phased groundwater monitoring. By October 17, 2017, electric utility companies that own or operate CCR disposal units, such as APS, must have collected sufficient groundwater sampling data to initiate a detection monitoring program. To the extent that certain threshold constituents are identified through this initial detection monitoring at levels above the CCR rule's standards, the rule required the initiation of an assessment monitoring program by April 15, 2018.

APS recently completed the statistical analyses for its CCR disposal units that triggered assessment monitoring. APS determined that several of its CCR disposal units at Cholla and Four Corners will need to undergo corrective action. In addition, all such units must cease operating and initiate closure by October of 2020. APS currently estimates that the additional incremental costs to complete this corrective action and closure work, along with the costs to develop replacement CCR disposal capacity, could be approximately \$5 million for both Cholla and Four Corners. APS initiated an assessment of corrective measures on January 14, 2019, and anticipates completing this assessment during the summer of 2019. During this assessment, APS will gather additional groundwater data, solicit input from the public, host public hearings, and select remedies. As such, this \$5 million cost estimate may change based upon APS's performance of the CCR rule's corrective action assessment process. Given uncertainties that may exist until we have fully completed the corrective

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action assessment process, we cannot predict any ultimate impacts to the Company; however, at this time we do not believe any potential change to the cost estimate would have a material impact on our financial position, results of operations or cash flows.

Clean Power Plan. On June 2, 2014, EPA issued two proposed rules to regulate greenhouse gas ("GHG") emissions from modified and reconstructed EGUs pursuant to Section 111(b) of the Clean Air Act and existing fossil fuel-fired power plants pursuant to Clean Air Act Section 111(d). On August 3, 2015, EPA finalized carbon pollution standards for EGUs, the "Clean Power Plan". On October 10, 2017, EPA issued a proposal to repeal the Clean Power Plan and proposed replacement regulations on August 21, 2018. In addition, judicial challenges to the Clean Power Plan are pending before the D.C. Circuit, though that litigation is currently in abeyance while EPA develops regulatory action to potentially repeal and replace that regulation.

EPA's pending proposal to regulate carbon emissions from EGUs replaces the Clean Power Plan with standards that are based entirely upon measures that can be implemented to improve the heat rate of steam-electric power plants, specifically coal-fired EGUs. In contrast with the Clean Power Plan, EPA's proposed "Affordable Clean Energy Rule" would not involve utility-level generation dispatch shifting away from coal-fired generation and toward renewable energy resources and natural gas-fired combined cycle power plants. In addition, to address the New Source Review ("NSR") implications of power plant upgrades potentially necessary to achieve compliance with the proposed Affordable Clean Energy Rule standards, EPA also proposed to revise EPA's NSR regulations to more readily authorize the implementation of EGU efficiency upgrades.

We cannot predict the outcome of EPA's regulatory actions related to the August 2015 carbon pollution standards for EGU's, including any actions related to EPA's repeal proposal for the Clean Power Plan or additional rulemaking actions to approve the EPA's recently proposed Affordable Clean Energy Rule. In addition, we cannot predict whether the D.C. Circuit Court will continue to hold the litigation challenging the original Clean Power Plan in abeyance in light of EPA's repeal proposal, which is still pending.

Other environmental rules that could involve material compliance costs include those related to effluent limitations, the ozone national ambient air quality standard and other rules or matters involving the Clean Air Act, Clean Water Act, Endangered Species Act, RCRA, Superfund, the Navajo Nation, and water supplies for our power plants. The financial impact

of complying with current and future environmental rules could jeopardize the economic viability of our coal plants or the willingness or ability of power plant participants to fund any required equipment upgrades or continue their participation in these plants. The economics of continuing to own certain resources, particularly our coal plants, may deteriorate, warranting early retirement of those plants, which may result in asset impairments. APS would seek recovery in rates for the book value of any remaining investments in the plants as well as other costs related to early retirement, but cannot predict whether it would obtain such recovery.

Federal Agency Environmental Lawsuit Related to Four Corners

On April 20, 2016, several environmental groups filed a lawsuit against OSM and other federal agencies in the District of Arizona in connection with their issuance of the approvals that extended the life of Four Corners and the adjacent mine. The lawsuit alleges that these federal agencies violated both the Endangered Species Act ("ESA") and the National Environmental Policy Act ("NEPA") in providing the federal approvals necessary to extend operations at the Four Corners Power Plant and the adjacent Navajo Mine past July 6, 2016. APS filed a motion to intervene in the proceedings, which was granted on August 3, 2016.

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On September 15, 2016, NTEC, the company that owns the adjacent mine, filed a motion to intervene for the purpose of dismissing the lawsuit based on NTEC's tribal sovereign immunity. On September 11, 2017, the Arizona District Court issued an order granting NTEC's motion, dismissing the litigation with prejudice, and terminating the proceedings. On November 9, 2017, the environmental group plaintiffs appealed the district court order dismissing their lawsuit. Oral argument for this appeal has been scheduled for March 2019. We cannot predict whether this appeal will be successful and, if it is successful, the outcome of further district court proceedings.

Four Corners National Pollutant Discharge Elimination System ("NPDES") Permit

On July 16, 2018, several environmental groups filed a petition for review before the EPA Environmental Appeals Board ("EAB") concerning the NPDES wastewater discharge permit for Four Corners, which was reissued on June 12, 2018. The environmental groups allege that the permit was reissued in contravention of several requirements under the Clean Water Act and did not contain required provisions concerning EPA's 2015 revised effluent limitation guidelines for steam-electric EGUs, 2014 existing-source regulations governing cooling-water intake structures, and effluent limits for surface seepage and subsurface discharges from coal-ash disposal facilities. To address certain of these issues through a reconsidered permit, EPA took action on December 19, 2018 to withdraw the NPDES permit reissued in June 2018. Withdrawal of the permit moots the EAB appeal, and EPA filed a motion to dismiss on that basis. EPA indicated that it anticipates proposing a replacement NPDES permit by March 2019 and, depending on the extent of public comments concerning that proposal, taking final action on a new NPDES permit by June 2019. At this time, we cannot predict the outcome of EPA's reconsideration of the NPDES permit and whether reconsideration will have a material impact on our financial position, results of operations or cash flows.

Four Corners Coal Supply Agreement

Arbitration

On June 13, 2017, APS received a Demand for Arbitration from NTEC in connection with the Coal Supply Agreement, dated December 30, 2013, under which NTEC supplies coal to APS and the other Four Corners owners (collectively, the "Buyer") for use at the Four Corners Power Plant (the "2016 Coal Supply Agreement"). NTEC was originally seeking a

declaratory judgment to support its interpretation of a provision regarding uncontrollable forces in the agreement that relates to annual minimum quantities of coal to be purchased by the Buyer. NTEC also alleged a shortfall in the Buyer's purchases for the initial contract year of approximately \$30 million. APS's share of this amount is approximately \$17 million. On September 20, 2017, NTEC amended its Demand for Arbitration, removing its request for a declaratory judgment and at such time was only seeking relief for the alleged shortfall in the Buyer's purchases for the initial contract year.

On June 29, 2018, the parties settled the dispute for \$45 million, which includes settlement for the initial contract year and the current contract year. APS's share of this amount is approximately \$34 million. In connection with the settlement, the parties amended the 2016 Coal Supply Agreement, including modifying the provisions that gave rise to this dispute. (See "4CA Matter" below for additional matters agreed to between 4CA and NTEC in the settlement arrangement.) The arbitration was dismissed on July 9, 2018.

Coal Advance Purchase

On March 12, 2018, APS paid to NTEC approximately \$24 million as an advance payment for APS's share of coal under the 2016 Coal Supply Agreement. The coal inventory purchased represents an amount that APS expects to use for its plant operations within the next year.

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****4CA Matter**

On July 6, 2016, 4CA purchased El Paso's 7% interest in Four Corners. NTEC had the option to purchase the 7% interest within a certain timeframe pursuant to an option granted to NTEC. On December 29, 2015, NTEC provided notice of its intent to exercise the option. The purchase did not occur during the originally contemplated timeframe. Concurrent with the settlement of the 2016 Coal Supply Agreement matter described above, NTEC and 4CA agreed to allow for the purchase by NTEC of the 7% interest, consistent with the option. On June 29, 2018, 4CA and NTEC entered into an asset purchase agreement providing for the sale to NTEC of 4CA's 7% interest in Four Corners. Completion of the sale was subject to the receipt of approval by FERC, which was received on July 2, 2018, and the sale transaction closed on July 3, 2018. NTEC purchased the 7% interest at 4CA's book value, approximately \$70 million, and will pay 4CA the purchase price over a period of four years pursuant to a secured interest-bearing promissory note. In connection with the sale, Pinnacle West guaranteed certain obligations that NTEC will have to the other owners of Four Corners, such as NTEC's 7% share of capital expenditures and operating and maintenance expenses. Pinnacle West's guarantee is secured by a portion of APS's payments to be owed to NTEC under the 2016 Coal Supply Agreement.

The 2016 Coal Supply Agreement contained alternate pricing terms for the 7% interest in the event NTEC did not purchase the interest. Until the time that NTEC purchased the 7% interest, the alternate pricing provisions were applicable to 4CA as the holder of the 7% interest. These terms included a formula under which NTEC must make certain payments to 4CA for reimbursement of operations and maintenance costs and a specified rate of return, offset by revenue generated by 4CA's power sales. Such payments are due to 4CA at the end of each calendar year. A \$10 million payment was due to 4CA at December 31, 2017, which NTEC satisfied by directing to 4CA a prepayment from APS of a portion of a future mine reclamation obligation. The balance of the amount under this formula due December 31, 2018 for calendar year 2017 is approximately \$20 million, which was paid to 4CA on December 14, 2018. The balance of the amount under this formula at December 31, 2018 for calendar year 2018 (up to the date that NTEC purchased the 7% interest) is approximately \$10 million, which is due to 4CA at December 31, 2019.

Financial Assurances

In the normal course of business, we obtain standby letters of credit and surety bonds from financial institutions and other third parties. These instruments guarantee our own future

performance and provide third parties with financial and performance assurance in the event we do not perform. These instruments support certain commodity contract collateral obligations and other transactions. As of December 31, 2018, standby letters of credit totaled \$0.2 million and will expire in 2019. As of December 31, 2018, surety bonds expiring through 2019 totaled \$17 million. The underlying liabilities insured by these instruments are reflected on our balance sheets, where applicable. Therefore, no additional liability is reflected for the letters of credit and surety bonds themselves.

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.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Pinnacle West has issued parental guarantees and has provided indemnification under certain surety bonds for APS which were not material at December 31, 2018. Since July 6, 2016, Pinnacle West has issued five parental guarantees for 4CA relating to payment obligations arising from 4CA's acquisition of El Paso's 7% interest in Four Corners, and pursuant to the Four Corners participation agreement payment obligations arising from 4CA's ownership interest in Four Corners, four of which terminated following the sale of 4CA's 7% interest to NTEC. (See "Four Corners Coal Supply Agreement - 4CA Matter" above for information related to this sale.)

In connection with the sale of 4CA's 7% interest to NTEC, Pinnacle West is guaranteeing certain obligations that NTEC will have to the other owners of Four Corners. (See "Four Corners Coal Supply Agreement - 4CA Matter" above for information related to this guarantee.) A maximum obligation is not explicitly stated in the guarantee and, therefore, the overall maximum amount of the obligation under such guarantee cannot be reasonably estimated; however, we consider the fair value of this guarantee to be immaterial.

11. Asset Retirement Obligations

In 2018, APS recognized an ARO for the removal of hazardous waste containing solar panels at all of our utility scale solar plants, which resulted in an increase to the ARO in the amount of \$14 million. In addition, due to the sale of 4CA assets to NTEC in 2018 (see Note 10 for more information on 4CA matters) there was a decrease to the ARO of \$9 million. APS recognized an ARO of \$7 million for rooftop solar removals in accordance with the obligations included in the customer contracts, which requires APS to remove the panels at the end of the contract life and includes the costs for the disposal of hazardous materials in accordance with environmental regulations. Finally, APS has other ARO adjustments resulting in a net decrease of \$1 million.

In 2017, APS received a new decommissioning study for the Navajo Plant. This resulted in an increase to the ARO in the amount of \$22 million, an increase in regulatory asset of \$2 million and a reduction of the regulatory liability of \$20 million.

The following table shows the change in our asset retirement obligations for 2018 and 2017 (dollars in thousands):

	2018	2017
Asset retirement obligations at the beginning of year	\$679,529	\$624,475
Changes attributable to:		
Accretion expense	36,876	33,104
Settlements	(9,726)	—
Estimated cash flow revisions	2,002	21,950
Newly incurred or acquired obligations	17,864	—
Asset retirement obligations at the end of year	\$726,545	\$679,529

In accordance with regulatory accounting, APS accrues removal costs for its regulated utility assets, even if there is no legal obligation for removal. See detail of regulatory liabilities in Note 3.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**12. Selected Quarterly Financial Data (Unaudited)**

Consolidated quarterly financial information for 2018 and 2017 is provided in the tables below (dollars in thousands, except per share amounts). Weather conditions cause significant seasonal fluctuations in our revenues; therefore, results for interim periods do not necessarily represent results expected for the year.

	2018 Quarter Ended				2018
	March 31,	June 30,	September 30,	December 31,	Total
Operating revenues	\$692,714	\$974,123	\$1,268,034	\$756,376	\$3,691,247
Operations and maintenance	265,682	268,397	246,545	256,120	1,036,744
Operating income	31,334	242,162	433,307	66,884	773,687
Income taxes	(1,265)	44,039	84,333	6,795	133,902
Net income	8,094	171,612	319,885	30,949	530,540
Net income attributable to common shareholders	3,221	166,738	315,012	26,076	511,047

Earnings Per Share:

Net income attributable to common shareholders — Basic	\$0.03	\$1.49	\$2.81	\$0.23	\$4.56
Net income attributable to common shareholders — Diluted	0.03	1.48	2.80	0.23	4.54

	2017 Quarter Ended				2017
	March 31,	June 30,	September 30,	December 31,	Total
Operating revenues	\$677,728	\$944,587	\$1,183,322	\$759,659	\$3,565,296
Operations and maintenance	226,071	220,985	230,839	271,212	949,107
Operating income	67,411	297,257	459,548	85,547	909,763
Income taxes	4,211	88,967	144,319	20,775	258,272
Net income	28,185	172,317	280,945	26,502	507,949
Net income attributable to common shareholders	23,312	167,443	276,072	21,629	488,456

Earnings Per Share:

Net income attributable to common shareholders — Basic	\$0.21	\$1.50	\$2.47	\$0.19	\$4.37
Net income attributable to common shareholders — Diluted	0.21	1.49	2.46	0.19	4.35

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Selected Quarterly Financial Data (Unaudited) - APS**

APS's quarterly financial information for 2018 and 2017 is as follows (dollars in thousands):

	2018 Quarter Ended				2018
	March 31,	June 30,	September 30,	December 31,	Total
Operating revenues	\$692,006	\$971,963	\$1,267,997	\$756,376	\$3,688,342
Operations and maintenance	254,601	251,999	226,346	236,281	969,227
Operating income	37,878	251,590	453,547	86,753	829,768
Net income attributable to common shareholder	9,599	177,825	338,366	44,475	570,265

	2017 Quarter Ended				2017
	March 31,	June 30,	September 30,	December 31,	Total
Operating revenues	\$677,589	\$943,406	\$1,178,846	\$757,811	\$3,557,652
Operations and maintenance	219,008	215,775	222,374	260,826	917,983
Operating income	70,269	296,700	465,658	91,912	924,539
Net income attributable to common shareholder	23,162	169,108	284,256	27,783	504,309

13. Fair Value Measurements

We classify our assets and liabilities that are carried at fair value within the 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 — Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 — Other significant observable inputs, including 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 (such as yield curves).

Level 3 — Valuation models with significant unobservable inputs that are supported by little or no market activity. Instruments in this category include long-dated derivative transactions where valuations are unobservable due to the length of the transaction, options, and transactions in locations where observable market data does not exist. The valuation models we employ utilize spot prices, forward prices, historical market data and other factors to

forecast future prices.

Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Thus, a valuation may be classified in Level 3 even though the valuation may include significant inputs that are readily observable. We maximize the use of observable inputs and minimize the use of unobservable inputs. We rely primarily on the market approach of using prices and other market information for identical and/or comparable assets and liabilities. If market data is not readily available, inputs may reflect our own assumptions about the inputs market participants would use. Our assessment of the inputs and the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of fair value assets and liabilities as well as their placement within the fair value hierarchy levels. We assess whether a market is active by obtaining observable broker quotes, reviewing actual market activity, and assessing the volume of transactions. We consider broker quotes observable inputs when the quote is

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COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

binding on the broker, we can validate the quote with market activity, or we can determine that the inputs the broker used to arrive at the quoted price are observable.

Certain instruments have been valued using the concept of Net Asset Value ("NAV"), as a practical expedient. These instruments are typically structured as investment companies offering shares or units to multiple investors for the purpose of providing a return. These instruments are similar to mutual funds; however, their NAV is generally not published and publicly available, nor are these instruments traded on an exchange. Instruments valued using NAV, as a practical expedient are included in our fair value disclosures however, in accordance with GAAP are not classified within the fair value hierarchy levels.

Recurring Fair Value Measurements

We apply recurring fair value measurements to cash equivalents, derivative instruments, and investments held in the nuclear decommissioning trust and other special use funds. On an annual basis we apply fair value measurements to plan assets held in our retirement and other benefit plans. See Note 7 for fair value discussion of plan assets held in our retirement and other benefit plans.

Cash Equivalents

Cash equivalents represent certain investments in money market funds that are valued using quoted prices in active markets.

Risk Management Activities — Derivative Instruments

Exchange traded commodity contracts are valued using unadjusted quoted prices. For non-exchange traded commodity contracts, we calculate fair 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. 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 net exposure to counterparties, taking into account netting agreements, expected default experience for the credit rating of the counterparties and the overall diversification of the portfolio. We maintain credit policies that management believes

minimize overall credit risk.

Certain non-exchange traded commodity contracts are valued based on unobservable inputs due to the long-term nature of contracts, characteristics of the product, 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. We rely primarily on broker quotes to value these instruments. When our valuations utilize broker quotes, we perform various control procedures to ensure the quote has been developed consistent with fair value accounting guidance. These controls include assessing the quote for reasonableness by comparison against other broker quotes, reviewing historical price relationships, and assessing market activity. When broker quotes are not available, the primary valuation technique used to calculate the fair value is the extrapolation of forward pricing curves using observable market data for more liquid delivery points in the same region and actual transactions at more illiquid delivery points.

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.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Our energy risk management committee, consisting of officers and key management personnel, oversees our energy risk management activities to ensure compliance with our stated energy risk management policies. We have a risk control function that is responsible for valuing our derivative commodity instruments in accordance with established policies and procedures. The risk control function reports to the chief financial officer's organization.

Investments Held in Nuclear Decommissioning Trust and Other Special Use Funds

The nuclear decommissioning trust and other special use funds invest in fixed income and equity securities. Other special use funds include the coal reclamation escrow account and the active union medical trust. See Note 19 for additional discussion about our investment accounts.

We value investments in fixed income and equity securities using information provided by our trustees and escrow agent. Our trustees and escrow agent use pricing services that utilize the valuation methodologies described below to determine fair market value. We have internal control procedures designed to ensure this information is consistent with fair value accounting guidance. These procedures include assessing valuations using an independent pricing source, verifying that pricing can be supported by actual recent market transactions, assessing hierarchy classifications, comparing investment returns with benchmarks, and obtaining and reviewing independent audit reports on the trustees' and escrow agent's internal operating controls and valuation processes.

Fixed Income Securities

Fixed income securities issued by the U.S. Treasury are valued using quoted active market prices and are typically classified as Level 1. Fixed income securities issued by corporations, municipalities, and other agencies, including mortgage-backed instruments, are valued using quoted inactive market prices, quoted active market prices for similar securities, or by utilizing calculations which incorporate observable inputs such as yield curves and spreads relative to such yield curves. These fixed income instruments are classified as Level 2. Whenever possible, multiple market quotes are obtained which enables a cross-check validation. A primary price source is identified based on asset type, class, or issue of securities.

Fixed income securities may also include short-term investments in certificates of deposit, variable rate notes, time deposit accounts, U.S. Treasury and Agency obligations, U.S. Treasury repurchase agreements, commercial paper, and other short term instruments. These instruments are valued using active market prices or utilizing observable inputs described above.

Equity Securities

The nuclear decommissioning trust's equity security investments are held indirectly through commingled funds. The commingled funds are valued using the funds' NAV as a practical expedient. The funds' NAV is primarily derived from the quoted active market prices of the underlying equity securities held by the funds. We may transact in these commingled funds on a semi-monthly basis at the NAV. The commingled funds are maintained by a bank and hold investments in accordance with the stated objective of tracking the performance of the S&P 500 Index. Because the commingled funds' shares are offered to a limited group of investors, they are not considered to be traded in an active market. As these instruments are valued using NAV, as a practical expedient, they have not been classified within the fair value hierarchy.

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The nuclear decommissioning trust and other special use funds may also hold equity securities that include exchange traded mutual funds and money market accounts for short-term liquidity purposes. These short-term, highly-liquid, investments are valued using active market prices.

Fair Value Tables

The following table presents the fair value at December 31, 2018 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Other	Balance at December 31, 2018
Assets					
Cash equivalents	\$ 1,200	\$—	\$—	\$—	\$ 1,200
Risk management activities — derivative instruments:					
Commodity contracts	—	3,140	2	(2,029)	(a) 1,113
Nuclear decommissioning trust:					
Equity securities	5,203	—	—	2,148	(b) 7,351
U.S. commingled equity funds	—	—	—	396,805	(c) 396,805
U.S. Treasury debt	148,173	—	—	—	148,173
Corporate debt	—	96,656	—	—	96,656
Mortgage-backed debt securities	—	113,115	—	—	113,115
Municipal bonds	—	79,073	—	—	79,073
Other fixed income	—	9,961	—	—	9,961
Subtotal nuclear decommissioning trust	153,376	298,805	—	398,953	851,134
Other special use funds:					
Equity securities	45,130	—	—	593	(b) 45,723
U.S. Treasury debt	173,310	—	—	—	173,310
Municipal bonds	—	17,068	—	—	17,068
Subtotal other special use funds	218,440	17,068	—	593	236,101
Total Assets	\$ 373,016	\$ 319,013	\$ 2	\$ 397,517	\$ 1,089,548
Liabilities					
Risk management activities — derivative instruments:					
Commodity contracts	\$—	\$(52,696)	\$(8,216)	\$ 875	(a) \$(60,037)

(a) Represents counterparty netting, margin, and collateral. See Note 16.

(b) Represents net pending securities sales and purchases.

(c)

Valued using NAV as a practical expedient and, therefore, are not classified in the fair value hierarchy.

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The following table presents the fair value at December 31, 2017 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (a) (Level 3)	Other	Balance at December 31, 2017
Assets					
Cash equivalents	\$ 10,630	\$—	\$—	\$—	\$ 10,630
Risk management activities — derivative instruments:					
Commodity contracts	—	5,683	1,036	(4,737)	(b) 1,982
Nuclear decommissioning trust:					
Cash and cash equivalents	7,224	—	—	109	(d) 7,333
U.S. commingled equity funds	—	—	—	417,390	(e) 417,390
U.S. Treasury debt	127,662	—	—	—	127,662
Corporate debt	—	114,007	—	—	114,007
Mortgage-backed debt securities	—	111,874	—	—	111,874
Municipal bonds	—	79,049	—	—	79,049
Other fixed income	—	13,685	—	—	13,685
Subtotal nuclear decommissioning trust	134,886	318,615	—	417,499	871,000
Other special use funds (c):	455	31,562	—	525	32,542
Total Assets	\$ 145,971	\$ 355,860	\$ 1,036	\$ 413,287	\$ 916,154
Liabilities					
Risk management activities — derivative instruments:					
Commodity contracts	\$—	\$(78,646)	\$(19,292)	\$ 1,516	(b) \$(96,422)
(a) Primarily consists of long-dated electricity contracts.					
(b) Represents counterparty netting, margin, and collateral. See Note 16.					
(c) Primarily consists of fixed income municipal bonds. Presented as coal reclamation escrow in 2017.					
(d) Represents nuclear decommissioning trust net pending securities sales and purchases.					
(e) Valued using NAV as a practical expedient and, therefore, are not classified in the fair value hierarchy.					

Fair Value Measurements Classified as Level 3

The significant unobservable inputs used in the fair value measurement of our energy derivative contracts include broker quotes that cannot be validated as an observable input primarily due to the long-term nature of the quote. Significant changes in these inputs in isolation would result in significantly higher or lower fair value measurements. Changes in

our derivative contract fair values, including changes relating to unobservable inputs, typically will not impact net income due to regulatory accounting treatment (see Note 3).

Because our forward commodity contracts classified as Level 3 are currently in a net purchase position, we would expect price increases of the underlying commodity to result in increases in the net fair value of the

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related contracts. Conversely, if the price of the underlying commodity decreases, the net fair value of the related contracts would likely decrease.

Other unobservable valuation inputs include credit and liquidity reserves which do not have a material impact on our valuations; however, significant changes in these inputs could also result in higher or lower fair value measurements.

The following tables provide information regarding our significant unobservable inputs used to value our risk management derivative Level 3 instruments at December 31, 2018 and December 31, 2017:

Commodity Contracts	December 31, 2018		Valuation Technique	Significant Unobservable Input	Range	Weighted-Average
	Fair Value (thousands)					
	Assets	Liabilities				
Electricity:						
Forward Contracts (a)	\$—	\$2,456	Discounted cash flows	Electricity forward price (per MWh)	\$17.88 - \$37.03	\$ 26.10
Natural Gas:						
Forward Contracts (a)	2	5,760	Discounted cash flows	Natural gas forward price (per MMBtu)	\$1.79 - \$2.92	\$ 2.48
Total	\$2	\$8,216				

(a) Includes swaps and physical and financial contracts.

Commodity Contracts	December 31, 2017		Valuation Technique	Significant Unobservable Input	Range	Weighted-Average
	Fair Value (thousands)					
	Assets	Liabilities				
Electricity:						
Forward Contracts (a)	\$21	\$15,485	Discounted cash flows	Electricity forward price (per MWh)	\$18.51 - \$38.75	\$ 27.89
Natural Gas:						
Forward Contracts (a)	1,015	3,807	Discounted cash flows	Natural gas forward price (per MMBtu)	\$2.33 - \$3.11	\$ 2.71
Total	\$1,036	\$19,292				

(a) Includes swaps and physical and financial contracts.

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The following table shows the changes in fair value for our risk management activities' assets and liabilities that are measured at fair value on a recurring basis using Level 3 inputs for the years ended December 31, 2018 and 2017 (dollars in thousands):

	Year Ended December 31,	
	2018	2017
Commodity Contracts		
Net derivative balance at beginning of period	\$(18,256)	\$(47,406)
Total net gains (losses) realized/unrealized:		
Included in earnings	—	—
Included in OCI	—	3
Deferred as a regulatory asset or liability	(1,130)	(13,643)
Settlements	(787)	5,834
Transfers into Level 3 from Level 2	(12,830)	(10,026)
Transfers from Level 3 into Level 2	24,789	46,982
Net derivative balance at end of period	\$(8,214)	\$(18,256)
Net unrealized gains included in earnings related to instruments still held at end of period	\$—	\$—

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

Financial Instruments Not Carried at Fair Value

The carrying value of our short-term borrowings approximate fair value and are classified within Level 2 of the fair value hierarchy. See Note 6 for our long-term debt fair values. The NTEC note receivable related to the sale of 4CA's interest in Four Corners bears interest at 3.9% per annum and has a book value of \$61 million as of December 31, 2018, as presented on the Consolidated Balance Sheets. The carrying amount is not materially different from the fair value of the note receivable and is classified within Level 3 of the fair value hierarchy. See Note 10 for more information on 4CA matters.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**14. Earnings Per Share**

The following table presents the calculation of Pinnacle West's basic and diluted earnings per share for continuing operations attributable to common shareholders for the years ended December 31, 2018, 2017 and 2016 (in thousands, except per share amounts):

	2018	2017	2016
Net income attributable to common shareholders	\$511,047	\$488,456	\$442,034
Weighted average common shares outstanding — basic	112,129	111,839	111,409
Net effect of dilutive securities:			
Contingently issuable performance shares and restricted stock units	421	528	637
Weighted average common shares outstanding — diluted	112,550	112,367	112,046
Earnings per weighted-average common share outstanding			
Net income attributable to common shareholders - basic	\$4.56	\$4.37	\$3.97
Net Income attributable to common shareholders - diluted	\$4.54	\$4.35	\$3.95

15. Stock-Based Compensation

Pinnacle West has incentive compensation plans under which stock-based compensation is granted to officers, key-employees, and non-officer members of the Board of Directors. Awards granted under the 2012 Long-Term Incentive Plan ("2012 Plan") may be in the form of stock grants, restricted stock units, stock units, performance shares, restricted stock, dividend equivalents, performance share units, performance cash, incentive and non-qualified stock options, and stock appreciation rights. The 2012 Plan authorizes up to 4.6 million common shares to be available for grant. As of December 31, 2018, 1.9 million common shares were available for issuance under the 2012 Plan. During 2018, 2017, and 2016, the Company granted awards in the form of restricted stock units, stock units, stock grants, and performance shares. Awards granted from 2007 to 2011 were issued under the 2007 Long-Term Incentive Plan ("2007 Plan"), and no new awards may be granted under the 2007 Plan.

Stock-Based Compensation Expense and Activity

Compensation cost included in net income for stock-based compensation plans was \$20 million in 2018, \$21 million in 2017, and \$19 million in 2016. The compensation cost capitalized is immaterial for all years. Income tax benefits related to stock-based compensation arrangements were \$7 million in 2018, \$15 million in 2017, and \$10 million in 2016.

As of December 31, 2018, there were approximately \$9 million of unrecognized compensation costs related to nonvested stock-based compensation arrangements. We expect to recognize these costs over a weighted-average period of 2 years.

The total fair value of shares vested was \$24 million in 2018, \$22 million in 2017 and \$22 million in 2016.

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The following table is a summary of awards granted and the weighted-average grant date fair value for the three years ended 2018, 2017 and 2016:

	Restricted Stock Units, Stock Grants, and Performance Shares (b) Stock Units (a)					
	2018	2017	2016	2018	2017	2016
Units granted	132,997	161,963	141,811	171,708	147,706	166,666
Weighted-average grant date fair value	\$77.51	\$72.60	\$67.34	\$76.56	\$78.99	\$66.60

(a) Units granted includes awards that will be cash settled of 66,252 in 2018, 67,599 in 2017, and 43,952 in 2016.

(b) Reflects the target payout level.

The following table is a summary of the status of non-vested awards as of December 31, 2018 and changes during the year:

	Restricted Stock Units, Stock Grants, and Stock Units		Performance Shares	
	Shares	Weighted-Average Grant Date Fair Value	Shares (b)	Weighted-Average Grant Date Fair Value
Nonvested at January 1, 2018	291,288	\$ 69.78	309,502	\$ 72.46
Granted	132,997	77.51	171,708	76.56
Vested	(147,938)	67.12	(159,284)	66.61
Forfeited (c)	(5,356)	73.42	(9,542)	73.34
Nonvested at December 31, 2018	270,991	(a)74.39	312,384	77.67
Vested Awards Outstanding at December 31, 2018	73,144		159,284	

(a) Includes 148,131 of awards that will be cash settled.

(b) The nonvested performance shares are reflected at target payout level.

(c) We account for forfeitures as they occur.

Share-based liabilities paid relating to restricted stock units were \$4 million, \$4 million and \$3 million in 2018, 2017 and 2016, respectively. This includes cash used to settle restricted stock units of \$5 million, \$4 million and \$3 million in 2018, 2017 and 2016, respectively. Restricted stock units that are cash settled are classified as liability awards. All performance shares are classified as equity awards.

Restricted Stock Units, Stock Grants, and Stock Units

Restricted stock units are granted to officers and key employees. Restricted stock units typically vest and settle in equal annual installments over a 4-year period after the grant date. Vesting is typically dependent upon continuous service during the vesting period; however, awards granted to retirement-eligible employees will vest upon the employee's retirement. Awardees elect to receive payment in either 100% stock, 100% cash, or 50% in cash and 50% in stock. Restricted stock unit awards typically include a dividend equivalent feature. This feature allows each award to accrue dividend rights equal to the dividends they would have received had they directly owned the stock. Interest on dividend rights compounds quarterly. If the award is forfeited the employee is not entitled to the dividends on those shares.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In December 2012, the Company granted a retention award of 50,617 performance-linked restricted stock units to the Chairman of the Board and Chief Executive Officer of Pinnacle West. This award vested on December 31, 2016, because he remained employed with the Company through that date. The Board did increase the number of awards that vested by 33,745 restricted stock units, payable in stock because certain performance requirements were met. In February 2017, 84,362 restricted stock units were released.

Compensation cost for restricted stock unit awards is based on the fair value of the award, with the fair value being the market price of our stock on the measurement date. Restricted stock unit awards that will be settled in cash are accounted for as liability awards, with compensation cost initially calculated on the date of grant using the Company's closing stock price, and remeasured at each balance sheet date. Restricted stock unit awards that will be settled in shares are accounted for as equity awards, with compensation cost calculated using the Company's closing stock price on the date of grant. Compensation cost is recognized over the requisite service period based on the fair value of the award.

Stock grants are issued to non-officer members of the Board of Directors. They may elect to receive the stock grant, or to defer receipt until a later date and receive stock units in lieu of the stock grant. The members of the Board of Directors who elect to defer may elect to receive payment in either 100% stock, 100% cash, or 50% in cash and 50% in stock. Each stock unit is convertible to one share of stock. The stock units accrue dividend rights, equal to the amount of dividends the Directors would have received had they directly owned stock equal to the number of vested restricted stock units or stock units from the date of grant to the date of payment, plus interest compounded quarterly. The dividends and interest are paid, based on the Director's election, in either stock, cash, or 50% in cash and 50% in stock.

Performance Share Awards

Performance share awards are granted to officers and key employees. The awards contain two separate performance criteria that affect the number of shares that may be received if after the end of a 3-year performance period the performance criteria are met. For the first criteria, the number of shares that will vest is based on non-financial performance metrics (i.e., the metric component). The other criteria is based upon Pinnacle West's total shareholder return ("TSR") in relation to the TSR of other companies in a specified utility index (i.e., the TSR component). The exact number of shares issued will vary from 0% to

200% of the target award. Shares received include dividend rights paid in stock equal to the amount of dividends that recipients would have received had they directly owned stock, equal to the number of vested performance shares from the date of grant to the date of payment plus interest compounded quarterly. If the award is forfeited or if the performance criteria are not achieved, the employee is not entitled to the dividends on those shares.

Performance share awards are accounted for as equity awards, with compensation cost based on the fair value of the award on the grant date. Compensation cost relating to the metric component of the award is based on the Company's closing stock price on the date of grant, with compensation cost recognized over the requisite service period based on the number of shares expected to vest. Management evaluates the probability of meeting the metric component at each balance sheet date. If the metric component criteria are not ultimately achieved, no compensation cost is recognized relating to the metric component, and any previously recognized compensation cost is reversed. Compensation cost relating to the TSR component of the award is determined using a Monte Carlo simulation valuation model, with compensation cost recognized ratably over the requisite service period, regardless of the number of shares that actually vest.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**16. Derivative Accounting**

Derivative financial instruments are used to manage exposure to commodity price and transportation costs of electricity, natural gas, coal, emissions allowances and interest rates. Risks associated with market volatility are managed by utilizing various physical and financial derivative instruments, including futures, forwards, options and swaps. As part of our overall risk management program, we may use derivative instruments to hedge purchases and sales of electricity and fuels. Derivative instruments that meet certain hedge accounting criteria may be designated as cash flow hedges and are used to limit our exposure to cash flow variability on forecasted transactions. The changes in market value of such instruments have a high correlation to price changes in the hedged transactions. Derivative instruments are also entered into for economic hedging purposes. While economic hedges may mitigate exposure to fluctuations in commodity prices, these instruments have not been designated as accounting hedges. Contracts that have the same terms (quantities, delivery points and delivery periods) and for which power does not flow are netted, which reduces both revenues and fuel and purchased power costs in our Consolidated Statements of Income, but does not impact our financial condition, net income or cash flows.

Our derivative instruments, excluding those qualifying for a scope exception, are recorded on the balance sheet as an asset or liability and are measured at fair value. See Note 13 for a discussion of fair value measurements. Derivative instruments may qualify for the normal purchases and normal sales scope exception if they require physical delivery and the quantities represent those transacted in the normal course of business. Derivative instruments qualifying for the normal purchases and sales scope exception are accounted for under the accrual method of accounting and excluded from our derivative instrument discussion and disclosures below.

For its regulated operations, APS defers for future rate treatment 100% of the unrealized gains and losses on 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 Base Fuel Rate (see Note 3). Gains and losses from derivatives in the following tables represent the amounts reflected in income before the effect of PSA deferrals.

As of December 31, 2018 and 2017, we had the following outstanding gross notional volume of derivatives, which represent both purchases and sales (does not reflect net position):

Commodity	Unit of Measure	Quantity	
		December 31, 2018	December 31, 2017
Power	GWh	250	583
Gas	Billion cubic feet	218	240

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Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Gains and Losses from Derivative Instruments**

The following table provides information about gains and losses from derivative instruments in designated cash flow accounting hedging relationships during the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

Commodity Contracts	Financial Statement Location	Year Ended December 31,	
		2018	2017
Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)	OCI — derivative instruments	\$—	\$(59)
Loss Reclassified from Accumulated OCI into Income (Effective Portion Realized) (a)	Fuel and purchased power (b)	(2,000)	519

(a) During the years ended December 31, 2018, 2017, and 2016, we had no losses reclassified from accumulated OCI to earnings related to discontinued cash flow hedges.

(b) Amounts are before the effect of PSA deferrals.

During the next twelve months, we estimate that a net loss of \$1.5 million before income taxes will be reclassified from accumulated OCI as an offset to the effect of market price changes for the related hedged transactions. In accordance with the PSA, most of these amounts will be recorded as either a regulatory asset or liability and have no immediate effect on earnings.

The following table provides information about gains and losses from derivative instruments not designated as accounting hedging instruments during the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

Commodity Contracts	Financial Statement Location	Year Ended December 31,		
		2018	2017	2016
Net Gain (Loss) Recognized in Income	Operating revenues	\$(2,557)	\$(1,192)	\$771
Net Gain (Loss) Recognized in Income	Fuel and purchased power (a)	(12,951)	(87,991)	25,711
Total		\$(15,508)	\$(89,183)	\$26,482

(a) Amounts are before the effect of PSA deferrals.

Derivative Instruments in the Consolidated Balance Sheets

Our derivative transactions are typically executed under standardized or customized agreements, which include collateral requirements and, in the event of a default, would allow

for the netting of positive and negative exposures associated with a single counterparty. Agreements that allow for the offsetting of positive and negative exposures associated with a single counterparty are considered master netting arrangements. Transactions with counterparties that have master netting arrangements are offset and reported net on the Consolidated Balance Sheets. Transactions that do not allow for offsetting of positive and negative positions are reported gross on the Consolidated Balance Sheets.

We do not offset a counterparty's current derivative contracts with the counterparty's non-current derivative contracts, although our master netting arrangements would allow current and non-current positions

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to be offset in the event of a default. Additionally, in the event of a default, our master netting arrangements would allow for the offsetting of all transactions executed under the master netting arrangement. These types of transactions may include non-derivative instruments, derivatives qualifying for scope exceptions, trade receivables and trade payables arising from settled positions, and other forms of non-cash collateral (such as letters of credit). These types of transactions are excluded from the offsetting tables presented below.

As of December 31, 2017, we no longer have derivative instruments that are designated as cash flow hedging instruments.

The following tables provide information about the fair value of our risk management activities reported on a gross basis, and the impacts of offsetting as of December 31, 2018 and 2017. These amounts relate to commodity contracts and are located in the assets and liabilities from risk management activities lines of our Consolidated Balance Sheets.

As of December 31, 2018: (dollars in thousands)	Gross Recognized Derivatives (a)	Amounts Offset (b)	Net Recognized Derivatives	Other (c)	Amount Reported on Balance Sheet
Current assets	\$3,106	\$(2,149)	\$957	\$156	\$1,113
Investments and other assets	36	(36)	—	—	—
Total assets	3,142	(2,185)	957	156	1,113
Current liabilities	(36,345)	2,149	(34,196)	(1,310)	(35,506)
Deferred credits and other	(24,567)	36	(24,531)	—	(24,531)
Total liabilities	(60,912)	2,185	(58,727)	(1,310)	(60,037)
Total	\$(57,770)	\$—	\$(57,770)	\$(1,154)	\$(58,924)

(a) All of our gross recognized derivative instruments were subject to master netting arrangements.

(b) No cash collateral has been provided to counterparties, or received from counterparties, that is subject to offsetting.

Represents cash collateral and cash margin that is not subject to offsetting. Amounts relate to non-derivative instruments, derivatives qualifying for scope exceptions, or (c) collateral and margin posted in excess of the recognized derivative instrument. Includes cash collateral received from counterparties of \$1,310 and cash margin provided to counterparties of \$156.

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As of December 31, 2017: (dollars in thousands)	Gross Recognized Derivatives (a)	Amounts Offset (b)	Net Recognized Derivatives	Other (c)	Amount Reported on Balance Sheet
Current assets	\$5,427	\$(3,796)	\$1,631	\$300	\$1,931
Investments and other assets	1,292	(1,241)	51	—	51
Total assets	6,719	(5,037)	1,682	300	1,982
Current liabilities	(59,527)	3,796	(55,731)	(3,521)	(59,252)
Deferred credits and other	(38,411)	1,241	(37,170)	—	(37,170)
Total liabilities	(97,938)	5,037	(92,901)	(3,521)	(96,422)
Total	\$(91,219)	\$—	\$(91,219)	\$(3,221)	\$(94,440)

(a) All of our gross recognized derivative instruments were subject to master netting arrangements.

(b) No cash collateral has been provided to counterparties, or received from counterparties, that is subject to offsetting.

(c) Represents cash collateral and cash margin that is not subject to offsetting. Amounts relate to non-derivative instruments, derivatives qualifying for scope exceptions, or collateral and margin posted in excess of the recognized derivative instrument. Includes cash collateral received from counterparties of \$3,521 and cash margin provided to counterparties of \$300.

Credit Risk and Credit Related Contingent Features

We are exposed to losses in the event of nonperformance or nonpayment by counterparties and have risk management contracts with many counterparties. As of December 31, 2018, Pinnacle West has no counterparties with positive exposures of greater than 10% of risk management assets. 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 counterparties 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.

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. 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 or Fitch or Baa3 for Moody's).

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The following table provides information about our derivative instruments that have credit-risk-related contingent features at December 31, 2018 (dollars in thousands):

	December 31, 2018
Aggregate fair value of derivative instruments in a net liability position	\$60,912
Cash collateral posted	—
Additional cash collateral in the event credit-risk related contingent features were fully triggered (a)	56,876

(a) This amount is after counterparty netting and includes those contracts which qualify for scope exceptions, which are excluded from the derivative details above.

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 \$94 million if our debt credit ratings were to fall below investment grade.

17. Other Income and Other Expense

The following table provides detail of Pinnacle West's Consolidated other income and other expense for 2018, 2017 and 2016 (dollars in thousands):

	2018	2017	2016
Other income:			
Interest income	\$8,647	\$3,497	\$884
Debt return on Four Corners SCR deferral (Note 3)	16,153	354	—
Miscellaneous	96	155	17
Total other income	\$24,896	\$4,006	\$901
Other expense:			
Non-operating costs	\$(10,076)	\$(11,749)	\$(9,235)
Investment losses — net	(417)	(4,113)	(1,747)
Miscellaneous	(7,473)	(5,677)	(4,355)
Total other expense	\$(17,966)	\$(21,539)	\$(15,337)

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Other Income and Other Expense - APS**

The following table provides detail of APS's other income and other expense for 2018, 2017 and 2016 (dollars in thousands):

	2018	2017	2016
Other income:			
Interest income	\$6,496	\$2,504	\$261
Debt return on Four Corners SCR deferral (Note 3)	16,153	354	—
Miscellaneous	97	155	10
Total other income	\$22,746	\$3,013	\$271
Other expense:			
Non-operating costs	\$(9,462)	\$(10,825)	\$(8,455)
Miscellaneous	(5,830)	(3,088)	(2,099)
Total other expense	\$(15,292)	\$(13,913)	\$(10,554)

18. Palo Verde Sale Leaseback Variable Interest Entities

In 1986, APS entered into agreements with three separate VIE lessor trust entities in order to sell and lease back interests in Palo Verde Unit 2 and related common facilities. APS will retain the assets through 2023 under one lease and 2033 under the other two leases. APS will be required to make payments relating to these leases of approximately \$23 million annually for the period 2019 through 2023, and about \$16 million annually for the period 2024 through 2033. At the end of the lease period, APS will have the option to purchase the leased assets at their fair market value, extend the leases for up to two years, or return the assets to the lessors.

The leases' terms give APS the ability to utilize the assets for a significant portion of the assets' economic life, and therefore provide APS with the power to direct activities of the VIEs that most significantly impact the VIEs' economic performance. Predominantly due to the lease terms, APS has been deemed the primary beneficiary of these VIEs and therefore consolidates the VIEs.

As a result of consolidation, we eliminate lease accounting and instead recognize depreciation expense, resulting in an increase in net income of \$19 million for 2018, 2017 and 2016. The increase in net income is entirely attributable to the noncontrolling interests.

Income attributable to Pinnacle West shareholders is not impacted by the consolidation.

Our Consolidated Balance Sheets at December 31, 2018 and December 31, 2017 include the following amounts relating to the VIEs (dollars in thousands):

	December 31, 2018	December 31, 2017
Palo Verde sale leaseback property, plant and equipment, net of accumulated depreciation	\$ 105,775	\$ 109,645
Equity-Noncontrolling interests	125,790	129,040

Assets of the VIEs are restricted and may only be used for payment to the noncontrolling interest holders. These assets are reported on our consolidated financial statements.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

APS is exposed to losses relating to these VIEs upon the occurrence of certain events that APS does not consider 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 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 were to occur during the lease periods, APS may be required to pay the noncontrolling equity participants approximately \$297 million beginning in 2019, and up to \$456 million over the lease extension term.

For regulatory ratemaking purposes, the agreements continue to be treated as operating leases and, as a result, we have recorded a regulatory asset relating to the arrangements.

19. Investments in Nuclear Decommissioning Trusts and Other Special Use Funds

We have investments in debt and equity securities held in Nuclear Decommissioning Trusts, Coal Reclamation Escrow Accounts, and an Active Union Employee Medical Account. Investments in debt securities are classified as available-for-sale securities. We record both debt and equity security investments at their fair value on our Consolidated Balance Sheets. See Note 13 for a discussion of how fair value is determined and the classification of the investments within the fair value hierarchy. The investments in each trust or account are restricted for use and are intended to fund specified costs and activities as further described for each fund below.

Nuclear Decommissioning Trusts - To fund the future costs APS expects to incur to decommission Palo Verde, APS established external decommissioning trusts in accordance with NRC regulations. Third-party investment managers are authorized to buy and sell securities per stated investment guidelines. The trust funds are invested in fixed income securities and equity securities. Earnings and proceeds from sales and maturities of securities are reinvested in the trusts. Because of the ability of APS to recover decommissioning costs in rates, and in accordance with the regulatory treatment, APS has deferred realized and unrealized gains and losses (including other-than-temporary impairments) in other regulatory liabilities.

Coal Reclamation Escrow Accounts - APS has investments restricted for the future coal mine reclamation funding related to Four Corners. This escrow account is primarily invested

in fixed income securities. Earnings and proceeds from sales of securities are reinvested in the escrow account. Because of the ability of APS to recover coal reclamation costs in rates, and in accordance with the regulatory treatment, APS has deferred realized and unrealized gains and losses (including other-than-temporary impairments) in other regulatory liabilities. Activities relating to APS coal reclamation escrow account investments are included within the other special use funds in the table below.

Active Union Employee Medical Account - APS has investments restricted for paying active union employee medical costs. These investments were transferred from APS other postretirement benefit trust assets into the active union employee medical trust in January 2018 (see Note 7). These investments may be used to pay active union employee medical costs incurred in the current period and in future periods. The account is invested primarily in fixed income securities. In accordance with the ratemaking treatment, APS has deferred the unrealized gains and losses (including other-than-temporary impairments) in other regulatory assets. Activities relating to active union employee medical account investments are included within the other special use funds in the table below.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**APS**

The following tables present the unrealized gains and losses based on the original cost of the investment and summarizes the fair value of APS's nuclear decommissioning trust and other special use fund assets at December 31, 2018 and December 31, 2017 (dollars in thousands):

Investment Type:	December 31, 2018			Total Unrealized Gains	Total Unrealized Losses
	Fair Value Nuclear Decommissioning Trusts	Other Special Use Funds	Total		
Equity Securities	\$402,008	\$45,130	\$447,138	\$222,147	\$(459)
Available for Sale-Fixed Income Securities	446,978	190,378	637,356	(a) 8,634	(6,778)
Other	2,148	593	2,741	(b) —	—
Total	\$851,134	\$236,101	\$1,087,235	\$230,781	\$(7,237)

(a) As of December 31, 2018, the amortized cost basis of these available-for-sale investments is \$635 million

(b) Represents net pending securities sales and purchases.

Investment Type:	December 31, 2017			Total Unrealized Gains	Total Unrealized Losses
	Fair Value Nuclear Decommissioning Trusts	Other Special Use Funds	Total		
Equity Securities	\$424,614	\$430	\$425,044	\$248,623	\$—
Available for Sale-Fixed Income Securities	446,277	29,439	475,716	(a) 11,537	(2,996)
Other	109	489	598	(b) —	—
Total	\$871,000	\$30,358	\$901,358	\$260,160	\$(2,996)

(a) As of December 31, 2017, the amortized cost basis of these available-for-sale investments is \$467 million.

(b) Represents net pending securities sales and purchases.

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The following table sets forth APS's realized gains and losses relating to the sale and maturity of available-for-sale debt securities and equity securities, and the proceeds from the sale and maturity of these investment securities for the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

	Year Ended December 31,		
	Nuclear Decommissioning Trusts	Other Special Commissioning Use Funds	Total
2018			
Realized gains	\$6,679	\$ 1	\$6,680
Realized losses	(13,552)	—	(13,552)
Proceeds from the sale of securities (a)	554,385	98,648	653,033
2017			
Realized gains	21,813	17	21,830
Realized losses	(13,146)	(9)	(13,155)
Proceeds from the sale of securities (a)	542,246	4,093	546,339
2016			
Realized gains	11,213	—	11,213
Realized losses	(10,106)	—	(10,106)
Proceeds from the sale of securities (a)	633,410	—	633,410

(a) Proceeds are reinvested in the nuclear decommissioning trusts or other special use funds.

Fixed Income Securities Contractual Maturities

The fair value of fixed income securities, summarized by contractual maturities, at December 31, 2018 is as follows (dollars in thousands):

	Nuclear Decommissioning	Coal Reclamation Escrow Accounts	Active Union Medical Trust	Total
Less than one year	\$ 26,819	\$ 21,237	\$39,966	\$88,022
1 year – 5 years	97,566	15,658	104,128	217,352
5 years – 10 years	128,379	2,511	—	130,890
Greater than 10 years	194,214	6,878	—	201,092
Total	\$ 446,978	\$ 46,284	\$ 144,094	\$637,356

20. Revenue

On January 1, 2018, we adopted new revenue guidance in ASU 2014-09 and related amendments. The new revenue guidance requires entities to recognize revenue when control of the promised good or service is transferred to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. We applied the new guidance using the modified retrospective method applied to contracts which were not completed as of January 1, 2018. The adoption of the new revenue guidance resulted in expanded disclosures but otherwise did not have a material impact on our financial statements. New revenue disclosures required by the standard are included below, and in Note 1. See Note 2 for additional information regarding the new accounting standard.

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The following table provides detail of Pinnacle West's consolidated revenue disaggregated by revenue sources (dollars in thousands):

	Year Ended December 31, 2018
Retail residential electric service	\$1,867,370
Retail non-residential electric service	1,628,891
Wholesale energy sales	109,198
Transmission services for others	60,261
Other sources	25,527
Total operating revenues	\$3,691,247

We derive our revenues from contracts with customers primarily from sales of electricity to our regulated retail customers. Our retail electric services and tariff rates are regulated by the ACC. Revenues from wholesale energy sales and transmission services for others represent energy and transmission sales to wholesale customers. Our wholesale activities and tariff rates are regulated by the FERC.

Revenue Activities

Our revenues are primarily derived from activities that are classified as revenues from contracts with customers. This includes sales of electricity to our regulated retail customers and wholesale and transmission activities. Our revenues from contracts with customers for the year ended December 31, 2018 were \$3,644 million.

We have certain revenues that do not meet the specific accounting criteria to be classified as revenues from contracts with customers. For the year ended December 31, 2018, our revenues that do not qualify as revenue from contracts with customers were \$47 million. This relates primarily to certain regulatory cost recovery mechanisms that are considered alternative revenue programs. We recognize revenue associated with alternative revenue programs when specific events permitting recognition are completed. Certain amounts associated with alternative revenue programs will subsequently be billed to customers; however, we do not reclassify billed amounts into revenue from contracts with customers. See Note 3 for a discussion of our regulatory cost recovery mechanisms.

Contract Assets and Liabilities from Contracts with Customers

There were no material contract assets, contract liabilities, or deferred contract costs recorded on the Consolidated Balance Sheets as of December 31, 2018.

Table of Contents**COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****21. Changes in Accumulated Other Comprehensive Loss**

The following table shows the changes in Pinnacle West's consolidated accumulated other comprehensive loss, including reclassification adjustments, net of tax, by component for the years ended December 31, 2018 and 2017 (dollars in thousands):

	Pension and Other Postretirement Benefits		Derivative Instruments	Total
Balance December 31, 2016	\$ (39,070 )	)	\$ (4,752)	\$(43,822)
OCI (loss) before reclassifications	(6,438 )	)	(35)	(6,473)
Amounts reclassified from accumulated other comprehensive loss	3,068	(a)	2,225	(b) 5,293
Balance December 31, 2017	(42,440 )	)	(2,562)	(45,002)
OCI (loss) before reclassifications	102	)	(78)	24
Amounts reclassified from accumulated other comprehensive loss	4,295	(a)	1,527	(b) 5,822
Reclassification of income tax effect related to tax reform	(7,954 )	)	(598)	(8,552)
Balance December 31, 2018	\$ (45,997 )	)	\$ (1,711)	\$(47,708)

(a) These amounts primarily represent amortization of actuarial loss, and are included in the computation of net periodic pension cost. See Note 7.

(b) These amounts represent realized gains and losses and are included in the computation of fuel and purchased power costs and are subject to the PSA. See Note 16.

Changes in Accumulated Other Comprehensive Loss - APS

The following table shows the changes in APS's consolidated accumulated other comprehensive loss, including reclassification adjustments, net of tax, by component for the years ended December 31, 2018 and 2017 (dollars in thousands):

	Pension and Other Postretirement Benefits		Derivative Instruments	Total
Balance December 31, 2016	\$ (20,671 )	)	\$ (4,752)	\$(25,423)
OCI (loss) before reclassifications	(6,884 )	)	(35)	(6,919)
Amounts reclassified from accumulated other comprehensive loss	3,134	(a)	2,225	(b) 5,359
Balance December 31, 2017	(24,421 )	)	(2,562)	(26,983)
OCI (loss) before reclassifications	(326 )	)	(78)	(404)
Amounts reclassified from accumulated other comprehensive loss	3,791	(a)	1,527	(b) 5,318
Reclassification of income tax effect related to tax reform	(4,440 )	)	(598)	(5,038)
Balance December 31, 2018	\$ (25,396 )	)	\$ (1,711)	\$(27,107)

- (a) These amounts primarily represent amortization of actuarial loss, and are included in the computation of net periodic pension cost. See Note 7.
- (b) These amounts represent realized gains and losses and are included in the computation of fuel and purchased power costs and are subject to the PSA. See Note 16.

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PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

(dollars in thousands)

	Year Ended December 31,		
	2018	2017	2016
Operating revenues	\$—	\$ 119	\$ 370
Operating expenses	53,844	24,591	26,573
Operating loss	(53,844)	(24,472)	(26,203)
Other			
Equity in earnings of subsidiaries	569,249	507,495	462,027
Other expense	(3,202)	(2,422)	(1,622)
Total	566,047	505,073	460,405
Interest expense	12,074	5,633	3,151
Income before income taxes	500,129	474,968	431,051
Income tax benefit	(10,918)	(13,488)	(10,983)
Net income attributable to common shareholders	511,047	488,456	442,034
Other comprehensive income (loss) — attributable to common shareholders	5,846	(1,180)	926
Total comprehensive income — attributable to common shareholders	\$ 516,893	\$ 487,276	\$ 442,960

See Combined Notes to Consolidated Financial Statements.

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PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT
CONDENSED BALANCE SHEETS

(dollars in thousands)

	December 31,	
	2018	2017
ASSETS		
Current assets		
Cash and cash equivalents	\$41	\$41
Accounts receivable	99,989	93,554
Income tax receivable	32,737	19,124
Other current assets	1,502	267
Total current assets	134,269	112,986
Investments and other assets		
Investments in subsidiaries	5,859,834	5,465,137
Deferred income taxes	5,243	54,352
Other assets	34,910	44,613
Total investments and other assets	5,899,987	5,564,102
Total Assets	\$6,034,256	\$5,677,088
LIABILITIES AND EQUITY		
Current liabilities		
Accounts payable	9,565	7,638
Accrued taxes	9,006	8,927
Common dividends payable	82,675	77,667
Short-term borrowings	76,400	95,400
Other current liabilities	19,215	17,417
Total current liabilities	196,861	207,049
Long-term debt less current maturities (Note 6)	448,796	298,421
Pension liabilities	17,766	20,758
Other	22,128	15,130
Total deferred credits and other	39,894	35,888
COMMITMENTS AND CONTINGENCIES (SEE NOTES)		
Common stock equity		
Common stock	2,629,440	2,609,181
Accumulated other comprehensive loss	(47,708)	(45,002)
Retained earnings	2,641,183	2,442,511
Total Pinnacle West Shareholders' equity	5,222,915	5,006,690
Noncontrolling interests	125,790	129,040
Total Equity	5,348,705	5,135,730
Total Liabilities and Equity	\$6,034,256	\$5,677,088

See Combined Notes to Consolidated Financial Statements.

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PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT
CONDENSED STATEMENTS OF CASH FLOWS

(dollars in thousands)

	Year Ended December 31,		
	2018	2017	2016
Cash flows from operating activities			
Net income	\$511,047	\$488,456	\$442,034
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in earnings of subsidiaries — net	(569,249)	(507,495)	(462,027)
Depreciation and amortization	76	76	85
Deferred income taxes	49,535	(264)	(12,402)
Accounts receivable	(7,881)	(2,106)	15,823
Accounts payable	1,967	(11,162)	10,402
Accrued taxes and income tax receivables — net	(13,535)	(22,247)	20,041
Dividends received from subsidiaries	316,000	296,800	239,300
Other	31,807	15,092	5,514
Net cash flow provided by operating activities	319,767	257,150	258,770
Cash flows from investing activities			
Construction work in progress	—	—	(18,457)
Investments in subsidiaries	(142,796)	(178,027)	(19,242)
Repayments of loans from subsidiaries	6,477	2,987	1,026
Advances of loans to subsidiaries	(500)	(6,388)	(2,092)
Net cash flow used for investing activities	(136,819)	(181,428)	(38,765)
Cash flows from financing activities			
Issuance of long-term debt	150,000	298,761	—
Short-term debt borrowings under revolving credit facility	20,000	58,000	40,000
Short-term debt repayments under revolving credit facility	(32,000)	(32,000)	—
Commercial paper - net	(7,000)	27,700	1,700
Dividends paid on common stock	(308,892)	(289,793)	(274,229)
Repayment of long-term debt	—	(125,000)	—
Common stock equity issuance - net of purchases	(5,055)	(13,390)	(4,867)
Other	(1)	—	—
Net cash flow used for financing activities	(182,948)	(75,722)	(237,396)
Net decrease in cash and cash equivalents	—	—	(17,391)
Cash and cash equivalents at beginning of year	41	41	17,432
Cash and cash equivalents at end of year	\$41	\$41	\$41

See Combined Notes to Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
NOTES TO FINANCIAL STATEMENTS OF HOLDING COMPANY

The Combined Notes to Consolidated Financial Statements in Part II, Item 8 should be read in conjunction with the Pinnacle West Capital Corporation Holding Company Financial Statements.

The Pinnacle West Capital Corporation Holding Company Financial Statements have been prepared to present the financial position, results of operations and cash flows of Pinnacle West Capital Corporation on a stand-alone basis as a holding company. Investments in subsidiaries are accounted for using the equity method.

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PINNACLE WEST CAPITAL CORPORATION
SCHEDULE II — RESERVE FOR UNCOLLECTIBLES
(dollars in thousands)

Column A	Column B	Column C	Column D	Column E	
Description	Balance at beginning of period	Additions		Deductions	Balance at end of period
		Charged to cost and expenses	Charged to other accounts		
Reserve for uncollectibles:					
2018	\$ 2,513	\$ 10,870	\$ —	—\$ 9,314	\$ 4,069
2017	3,037	6,836	—	7,360	2,513
2016	3,125	4,025	—	4,113	3,037

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ARIZONA PUBLIC SERVICE COMPANY
SCHEDULE II — RESERVE FOR UNCOLLECTIBLES

(dollars in thousands)

Column A	Column B	Column C	Column D	Column E	
Description	Balance at beginning of period	Additions		Deductions	Balance at end of period
		Charged to cost and expenses	Charged to other accounts		
Reserve for uncollectibles:					
2018	\$ 2,513	\$ 10,870	\$ —	—\$ 9,314	\$ 4,069
2017	3,037	6,836	—	7,360	2,513
2016	3,125	4,025	—	4,113	3,037

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. 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 (the “Exchange Act”) (15 U.S.C. 78a *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 December 31, 2018. 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’s management, with the participation of APS’s Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of APS’s disclosure controls and procedures as of December 31, 2018. Based on that evaluation, APS’s Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, APS’s disclosure controls and procedures were effective.

(b) Management’s Annual Reports on Internal Control Over Financial Reporting

Reference is made to “Management’s Report on Internal Control over Financial Reporting (Pinnacle West Capital Corporation)” in Item 8 of this report and “Management’s Report on Internal Control over Financial Reporting (Arizona Public Service Company)” in Item 8 of this report.

(c) Attestation Reports of the Registered Public Accounting Firm

Reference is made to “Report of Independent Registered Public Accounting Firm” in Item 8 of this report and “Report of Independent Registered Public Accounting Firm” in Item 8 of this report on the internal control over financial reporting of Pinnacle West and APS, respectively.

(d) Changes In Internal Control Over Financial Reporting

No change in Pinnacle West’s or APS’s internal control over financial reporting occurred during the fiscal quarter ended December 31, 2018 that materially affected, or is reasonably likely to materially affect, Pinnacle West’s or APS’s internal control over financial reporting.

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ITEM 9B. OTHER INFORMATION

None.

PART III

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS
AND CORPORATE GOVERNANCE OF PINNACLE WEST**

Reference is hereby made to “Information About Our Board and Corporate Governance,” “Proposal 1 — Election of Directors” and to “Section 16(a) Beneficial Ownership Reporting Compliance” in the Pinnacle West Proxy Statement relating to the Annual Meeting of Shareholders to be held on May 15, 2019 (the “2019 Proxy Statement”) and to the “Executive Officers of Pinnacle West” section in Part I of this report.

Pinnacle West has adopted a Code of Ethics for Financial Executives that applies to financial executives including Pinnacle West’s Chief Executive Officer, Chief Financial Officer, Chief Accounting Officer, Controller, Treasurer, and General Counsel, the President and Chief Operating Officer of APS and other persons designated as financial executives by the Chair of the Audit Committee. The Code of Ethics for Financial Executives is posted on Pinnacle West’s website (www.pinnaclewest.com). Pinnacle West intends to satisfy the requirements under Item 5.05 of Form 8-K regarding disclosure of amendments to, or waivers from, provisions of the Code of Ethics for Financial Executives by posting such information on Pinnacle West’s website.

ITEM 11. EXECUTIVE COMPENSATION

Reference is hereby made to “Directors’ Compensation,” “Executive Compensation,” and “Human Resources Committee Interlocks and Insider Participation” in the 2019 Proxy Statement.

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ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Reference is hereby made to “Ownership of Pinnacle West Stock” in the 2019 Proxy Statement.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth information as of December 31, 2018 with respect to the 2012 Plan and the 2007 Plan, under which our equity securities are outstanding or currently authorized for issuance.

Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	1,350,003	—	1,862,883
Equity compensation plans not approved by security holders		—	
Total	1,350,003	—	1,862,883

This amount includes shares subject to outstanding performance share awards and restricted stock unit awards at the maximum amount of shares issuable under such awards. However, payout of the performance share awards is contingent on the Company (a) reaching certain levels of performance during a three-year performance period. If the performance criteria for these awards are not fully satisfied, the award recipient will receive less than the maximum number of shares available under these grants and may receive nothing from these grants.

The weighted-average exercise price in this column does not take performance share (b) awards or restricted stock unit awards into account, as those awards have no exercise price.

(c) Awards under the 2012 Plan can take the form of options, stock appreciation rights, restricted stock, performance shares, performance share units, performance cash, stock grants, stock units, dividend equivalents, and restricted stock units. Additional shares cannot be awarded under the 2007 Plan. However, if an award under the 2012 Plan is forfeited, terminated or canceled or expires, the shares subject to such award, to the extent

of the forfeiture, termination, cancellation or expiration, may be added back to the shares available for issuance under the 2012 Plan.

Equity Compensation Plans Approved By Security Holders

Amounts in column (a) in the table above include shares subject to awards outstanding under two equity compensation plans that were previously approved by our shareholders: (a) the 2007 Plan, which was approved by our shareholders at our 2007 annual meeting of shareholders and under which no new stock awards may be granted; and (b) the 2012 Plan, as amended, which was approved by our shareholders at our 2012 annual meeting of shareholders and the first amendment to the 2012 Plan was approved by our shareholders at our 2017 annual meeting of shareholders. See Note 15 of the Notes to Consolidated Financial Statements for additional information regarding these plans.

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Equity Compensation Plans Not Approved by Security Holders

The Company does not have any equity compensation plans under which shares can be issued that have not been approved by the shareholders.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Reference is hereby made to “Information About Our Board and Corporate Governance” and “Related Party Transactions” in the 2019 Proxy Statement.

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Table of Contents**ITEM 14. PRINCIPAL ACCOUNTANT
FEES AND SERVICES****Pinnacle West**

Reference is hereby made to “Accounting and Auditing Matters — Audit Fees and — Pre-Approval Policies” in the 2019 Proxy Statement.

APS

The following fees were paid to APS’s independent registered public accountants, Deloitte & Touche LLP, for the last two fiscal years:

Type of Service	2018	2017
Audit Fees (1)	\$2,342,455	\$2,212,137
Audit-Related Fees (2)	300,334	292,467

(1) The aggregate fees billed for services rendered for the audit of annual financial statements and for review of financial statements included in Reports on Form 10-Q.

(2) The aggregate fees billed for assurance and related services that are reasonably related to the performance of the audit or review of the financial statements and are not included in Audit Fees reported above, which primarily consist of fees for employee benefit plan audits performed in 2018 and 2017.

Pinnacle West’s Audit Committee pre-approves each audit service and non-audit service to be provided by APS’s registered public accounting firm. The Audit Committee has delegated to the Chair of the Audit Committee the authority to pre-approve audit and non-audit services to be performed by the independent public accountants if the services are not expected to cost more than \$50,000. The Chair must report any pre-approval decisions to the Audit Committee at its next scheduled meeting. All of the services performed by Deloitte & Touche LLP for APS in 2018 were pre-approved by the Audit Committee or the Chair consistent with the pre-approval policy.

Table of Contents**PART IV****ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES****Financial Statements and Financial Statement Schedules**

See the Index to Financial Statements and Financial Statement Schedule in Part II, Item 8.

Exhibits Filed

The documents listed below are being filed or have previously been filed on behalf of Pinnacle West or APS and are incorporated herein by reference from the documents indicated and made a part hereof. Exhibits not identified as previously filed are filed herewith.

Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
3.1	Pinnacle West	<u>Articles of Incorporation, restated as of May 21, 2008</u>	3.1 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File No. 1-8962	8/7/2008
3.2	Pinnacle West	<u>Pinnacle West Capital Corporation Bylaws, amended as of February 22, 2017</u>	3.1 to Pinnacle West/APS February 28, 2017 Form 8-K Report, File Nos. 1-8962 and 1-4473	2/28/2017
3.3	APS	Articles of Incorporation, restated as of May 25, 1988	4.2 to APS's Form 18 Registration Nos. 33-33910 and 33-55248 by means of September 24, 1993 Form 8-K Report, File No. 1-4473	9/29/1993
3.3.1	APS	<u>Amendment to the Articles of Incorporation of Arizona Public Service Company, amended May 16, 2012</u>	3.1 to Pinnacle West/APS May 22, 2012 Form 8-K Report, File Nos. 1-8962 and 1-4473	5/22/2012
3.4	APS	<u>Arizona Public Service Company Bylaws, amended as of December 16, 2008</u>	3.4 to Pinnacle West/APS December 31, 2008 Form 10-K, File No. 1-4473	2/20/2009
4.1	Pinnacle West	<u>Specimen Certificate of Pinnacle West Capital Corporation Common Stock, no par value</u>	4.1 to Pinnacle West June 20, 2017 Form 8-K Report, File No. 1-8962	6/20/2017
4.2				1/11/1995

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	Pinnacle West APS	<u>Indenture dated as of January 1, 1995 among APS and The Bank of New York Mellon, as Trustee</u>	4.6 to APS's Registration Statement Nos. 33-61228 and 33-55473 by means of January 1, 1995 Form 8-K Report, File No. 1-4473	
4.2a	Pinnacle West APS	<u>First Supplemental Indenture dated as of January 1, 1995</u>	4.4 to APS's Registration Statement Nos. 33-61228 and 33-55473 by means of January 1, 1995 Form 8-K Report, File No. 1-4473	1/11/1995
4.3	Pinnacle West APS	<u>Indenture dated as of November 15, 1996 between APS and The Bank of New York, as Trustee</u>	4.5 to APS's Registration Statements Nos. 33-61228, 33-55473, 33-64455 and 333- 15379 by means of November 19, 1996 Form 8-K Report, File No. 1-4473	11/22/1996

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
4.3a	Pinnacle West APS	<u>First Supplemental Indenture dated as of November 15, 1996</u>	4.6 to APS's Registration Statements Nos. 33-61228, 33-55473, 33-64455 and 333-15379 by means of November 19, 1996 Form 8-K Report, File No. 1-4473	11/22/1996
4.3b	Pinnacle West APS	<u>Second Supplemental Indenture dated as of April 1, 1997</u>	4.10 to APS's Registration Statement Nos. 33-55473, 33-64455 and 333-15379 by means of April 7, 1997 Form 8-K Report, File No. 1-4473	4/9/1997
4.3c	Pinnacle West APS	<u>Third Supplemental Indenture dated as of November 1, 2002</u>	10.2 to Pinnacle West's March 31, 2003 Form 10-Q Report, File No. 1-8962	5/15/2003
4.4	Pinnacle West	<u>Indenture dated as of December 1, 2000 between the Company and The Bank of New York, as Trustee, relating to Senior Unsecured Debt Securities</u>	4.1 to Pinnacle West's Registration Statement No. 333-52476	12/21/2000
4.4a	Pinnacle West	<u>Third Supplemental Indenture dated as of November 30, 2017</u>	4.1 to Pinnacle West November 30, 2017 Form 8-K Report, File No. 1-8962	11/30/2017
4.5	Pinnacle West	<u>Indenture dated as of December 1, 2000 between the Company and The Bank of New York, as Trustee, relating to Subordinated Unsecured Debt Securities</u>	4.2 to Pinnacle West's Registration Statement No. 333-52476	12/21/2000
4.6	Pinnacle West APS	<u>Indenture dated as of January 15, 1998 between APS and The Bank of New York Mellon Trust Company N.A. (successor to JPMorgan Chase Bank, N.A., formerly known as The Chase Manhattan Bank), as Trustee</u>	4.10 to APS's Registration Statement Nos. 333-15379 and 333-27551 by means of January 13, 1998 Form 8-K Report, File No. 1-4473	1/16/1998
4.6a	Pinnacle West APS	<u>Seventh Supplemental Indenture dated as of May 1, 2003</u>	4.1 to APS's Registration Statement No. 333-90824 by means of May 7, 2003 Form 8-K Report, File No. 1-4473	5/9/2003
4.6b	Pinnacle West APS	<u>Eighth Supplemental Indenture dated as of June 15, 2004</u>	4.1 to APS's Registration Statement No. 333-106772 by means of June 24, 2004 Form 8-K Report, File No. 1-4473	6/28/2004
4.6c	Pinnacle West APS	<u>Ninth Supplemental Indenture dated as of August 15, 2005</u>	4.1 to APS's Registration Statements Nos. 333-106772 and 333-121512 by means of August 17, 2005 Form 8-K Report, File No. 1-4473	8/22/2005
4.6d	APS			8/3/2006

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		<u>Tenth Supplemental Indenture dated as of August 1, 2006</u>	4.1 to APS's July 31, 2006 Form 8-K Report, File No. 1-4473	
4.6e	Pinnacle West APS	<u>Eleventh Supplemental Indenture dated as of February 26, 2009</u>	4.6e to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015
4.6f	Pinnacle West APS	<u>Twelfth Supplemental Indenture dated as of August 25, 2011</u>	4.6f to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015
4.6g	Pinnacle West APS	<u>Thirteenth Supplemental Indenture dated as of January 13, 2012</u>	4.6g to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
4.6h	Pinnacle West APS	<u>Fourteenth Supplemental Indenture dated as of January 10, 2014</u>	4.6h to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015
4.6i	Pinnacle West APS	<u>Fifteenth Supplemental Indenture dated as of June 18, 2014</u>	4.6i to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015
4.6j	Pinnacle West APS	<u>Sixteenth Supplemental Indenture dated as of January 12, 2015</u>	4.6j to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/20/2015
4.6k	Pinnacle West APS	<u>Seventeenth Supplemental Indenture dated as of May 19, 2015</u>	4.1 to Pinnacle West/APS May 14, 2015 Form 8-K Report, File Nos. 1-8962 and 1-4473	5/19/2015
4.6l	Pinnacle West APS	<u>Eighteenth Supplemental Indenture dated as of November 6, 2015</u>	4.1 to Pinnacle West/APS November 3, 2015 Form 8-K Report, File Nos. 1-8962 and 1-4473	11/6/2015
4.6m	Pinnacle West APS	<u>Nineteenth Supplemental Indenture dated as of May 6, 2016</u>	4.1 to Pinnacle West/APS May 3, 2016 Form 8-K Report, File Nos. 1-8962 and 1-4473	5/6/2016
4.6n	Pinnacle West APS	<u>Twentieth Supplemental Indenture dated as of September 20, 2016</u>	4.1 to Pinnacle West/APS September 15, 2016 Form 8-K Report, File Nos. 1-8962 and 1-4473	9/20/2016
4.6o	Pinnacle West APS	<u>Twenty-First Supplemental Indenture dated as of September 11, 2017</u>	4.1 to Pinnacle West/APS September 11, 2017 Form 8-K Report, File Nos. 1-8962 and 1-4473	9/11/2017
4.6p	Pinnacle West APS	<u>Twenty-Second Supplemental Indenture dated as of August 9, 2018</u>	4.1 to Pinnacle West/APS August 9, 2018 Form 8-K Report, File Nos. 1-8962 and 1-4473	8/9/2018
4.7	Pinnacle West	<u>Second Amended and Restated Pinnacle West Capital Corporation Investors Advantage Plan dated as of June 23, 2004</u>	4.4 to Pinnacle West's June 23, 2004 Form 8-K Report, File No. 1-8962	8/9/2004
4.7a	Pinnacle West	<u>Third Amended and Restated Pinnacle West Capital Corporation Investors Advantage Plan dated as of November 25, 2008</u>	4.1 to Pinnacle West's Form S-3 Registration Statement No. 333-155641, File No. 1-8962	11/25/2008

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4.8	Pinnacle West	Agreement, dated March 29, 1988, relating to the filing of instruments defining the rights of holders of long-term debt not in excess of 10% of the Company's total assets	4.1 to Pinnacle West's 1987 Form 10-K Report, File No. 1-8962	3/30/1988
4.8a	Pinnacle West APS	<u>Agreement, dated March 21, 1994, relating to the filing of instruments defining the rights of holders of APS long-term debt not in excess of 10% of APS's total assets</u>	4.1 to APS's 1993 Form 10-K Report, File No. 1-4473	3/30/1994
10.1.1	Pinnacle West APS	Two separate Decommissioning Trust Agreements (relating to PVGS Units 1 and 3, respectively), each dated July 1, 1991, between APS and Mellon Bank, N.A., as Decommissioning Trustee	10.2 to APS's September 30, 1991 Form 10-Q Report, File No. 1-4473	11/14/1991

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.1.1a	Pinnacle West APS	<u>Amendment No. 1 to Decommissioning Trust Agreement (PVGS Unit 1), dated as of December 1, 1994</u>	10.1 to APS's 1994 Form 10-K Report, File No. 1-4473	3/30/1995
10.1.1b	Pinnacle West APS	<u>Amendment No. 1 to Decommissioning Trust Agreement (PVGS Unit 3), dated as of December 1, 1994</u>	10.2 to APS's 1994 Form 10-K Report, File No. 1-4473	3/30/1995
10.1.1c	Pinnacle West APS	<u>Amendment No. 2 to APS Decommissioning Trust Agreement (PVGS Unit 1) dated as of July 1, 1991</u>	10.4 to APS's 1996 Form 10-K Report, File No. 1-4473	3/28/1997
10.1.1d	Pinnacle West APS	<u>Amendment No. 2 to APS Decommissioning Trust Agreement (PVGS Unit 3) dated as of July 1, 1991</u>	10.6 to APS's 1996 Form 10-K Report, File No. 1-4473	3/28/1997
10.1.1e	Pinnacle West APS	<u>Amendment No. 3 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of March 18, 2002</u>	10.2 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962	5/15/2002
10.1.1f	Pinnacle West APS	<u>Amendment No. 3 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of March 18, 2002</u>	10.4 to Pinnacle West's March 2002 Form 10-Q Report, File No. 1-8962	5/15/2002
10.1.1g	Pinnacle West APS	<u>Amendment No. 4 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of December 19, 2003</u>	10.3 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962	3/15/2004
10.1.1h	Pinnacle West APS	<u>Amendment No. 4 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of December 19, 2003</u>	10.5 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962	3/15/2004
10.1.1i	Pinnacle West APS	<u>Amendment No. 5 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of May 1, 2007</u>	10.1 to Pinnacle West/APS March 31, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/9/2007
10.1.1j	Pinnacle West APS	<u>Amendment No. 5 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of May 1, 2007</u>	10.2 to Pinnacle West/APS March 31, 2007 Form 10-Q Report, File Nos. 1-8962 and 104473	5/9/2007
10.1.2	Pinnacle West APS	Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2) dated as of January 31, 1992, among APS, Mellon Bank, N.A., as Decommissioning Trustee, and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee under two separate Trust Agreements,	10.1 to Pinnacle West's 1991 Form 10-K Report, File No. 1-8962	3/26/1992

each with a separate Equity Participant, and as Lessor under two separate Facility Leases, each relating to an undivided interest in PVGS Unit 2

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.1.2a	Pinnacle West APS	First Amendment to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of November 1, 1992	10.2 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
10.1.2b	Pinnacle West APS	<u>Amendment No. 2 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of November 1, 1994</u>	10.3 to APS's 1994 Form 10-K Report, File No. 1-4473	3/30/1995
10.1.2c	Pinnacle West APS	<u>Amendment No. 3 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of June 20, 1996</u>	10.1 to APS's June 30, 1996 Form 10-Q Report, File No. 1-4473	8/9/1996
10.1.2d	Pinnacle West APS	<u>Amendment No. 4 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2) dated as of December 16, 1996</u>	APS 10.5 to APS's 1996 Form 10-K Report, File No. 1-4473	3/28/1997
10.1.2e	Pinnacle West APS	<u>Amendment No. 5 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of June 30, 2000</u>	10.1 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962	5/15/2002
10.1.2f	Pinnacle West APS	<u>Amendment No. 6 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of March 18, 2002</u>	10.3 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962	5/15/2002
10.1.2g	Pinnacle West APS	<u>Amendment No. 7 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of December 19, 2003</u>	10.4 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962	3/15/2004
10.1.2h	Pinnacle West APS	<u>Amendment No. 8 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of April 1, 2007</u>	10.1.2h to Pinnacle West's 2007 Form 10-K Report, File No. 1-8962	2/27/2008
10.2.1 ^b	Pinnacle West APS	Arizona Public Service Company Deferred Compensation Plan, as restated, effective January 1, 1984, and the second and third amendments thereto, dated December 22, 1986, and December 23, 1987, respectively	10.4 to APS's 1988 Form 10-K Report, File No. 1-4473	3/8/1989
10.2.1a ^b	Pinnacle West APS	<u>Third Amendment to the Arizona Public Service Company Deferred Compensation Plan, effective as of January 1, 1993</u>	10.3A to APS's 1993 Form 10-K Report, File No. 1-4473	3/30/1994
10.2.1b ^b	Pinnacle West APS	<u>Fourth Amendment to the Arizona Public Service Company Deferred Compensation Plan effective as of May 1, 1993</u>	10.2 to APS's September 30, 1994 Form 10-Q Report, File No. 1-4473	11/10/1994
10.2.1c ^b	Pinnacle West	<u>Fifth Amendment to the Arizona Public Service Company Deferred Compensation Plan effective</u>	10.3A to APS's 1996 Form 10-K Report, File	3/28/1997

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APS	<u>January 1, 1997</u>	No. 1-4473	
10.2.1d ^b	<u>Sixth Amendment to the Arizona Public Service</u>	10.8A to Pinnacle West's 2000	
West	<u>Company Deferred Compensation Plan effective</u>	Form 10-K Report, File	3/14/2001
APS	<u>January 1, 2001</u>	No. 1-8962	

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.2.2 ^b	Pinnacle West APS	Arizona Public Service Company Directors' Deferred Compensation Plan, as restated, effective January 1, 1986	10.1 to APS's June 30, 1986 Form 10-Q Report, File No. 1-4473	8/13/1986
10.2.2a ^b	Pinnacle West APS	<u>Second Amendment to the Arizona Public Service Company Directors' Deferred Compensation Plan, effective as of January 1, 1993</u>	10.2A to APS's 1993 Form 10-K Report, File No. 1-4473	3/30/1994
10.2.2b ^b	Pinnacle West APS	<u>Third Amendment to the Arizona Public Service Company Directors' Deferred Compensation Plan, effective as of May 1, 1993</u>	10.1 to APS's September 30, 1994 Form 10-Q Report, File No. 1-4473	11/10/1994
10.2.2c ^b	Pinnacle West APS	<u>Fourth Amendment to the Arizona Public Service Company Directors Deferred Compensation Plan, effective as of January 1, 1999</u>	10.8A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962	3/30/2000
10.2.3 ^b	Pinnacle West APS	<u>Trust for the Pinnacle West Capital Corporation, Arizona Public Service Company and SunCor Development Company Deferred Compensation Plans dated August 1, 1996</u>	10.14A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962	3/30/2000
10.2.3a ^b	Pinnacle West APS	<u>First Amendment dated December 7, 1999 to the Trust for the Pinnacle West Capital Corporation, Arizona Public Service Company and SunCor Development Company Deferred Compensation Plans</u>	10.15A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962	3/30/2000
10.2.4 ^b	Pinnacle West APS	<u>Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan as amended and restated effective January 1, 1996</u>	10.10A to APS's 1995 Form 10-K Report, File No. 1-4473	3/29/1996
10.2.4a ^b	Pinnacle West APS	<u>First Amendment effective as of January 1, 1999, to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan</u>	10.7A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962	3/30/2000
10.2.4b ^b	Pinnacle West APS	<u>Second Amendment effective January 1, 2000 to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan</u>	10.10A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962	3/30/2000
10.2.4c ^b	Pinnacle West APS	<u>Third Amendment to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado</u>	10.3 to Pinnacle West's March 31, 2003 Form 10-Q Report, File No. 1-8962	5/15/2003

Investment Company Deferred Compensation Plan,
effective as of January 1, 2002

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.2.4 ^b	Pinnacle West APS	<u>Fourth Amendment to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan, effective January 1, 2003</u>	10.64b to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/13/2006
10.2.5 ^b	Pinnacle West APS	<u>Deferred Compensation Plan of 2005 for Employees of Pinnacle West Capital Corporation and Affiliates (as amended and restated effective January 1, 2016)</u>	10.2.5 to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/19/2016
10.3.1 ^b	Pinnacle West APS	<u>Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan, amended and restated as of January 1, 2003</u>	10.7A to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962	3/15/2004
10.3.1a ^b	Pinnacle West APS	<u>Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan, as amended and restated, dated December 18, 2003</u>	10.48b to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/13/2006
10.3.2 ^b	Pinnacle West APS	<u>Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016)</u>	10.3.2 to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/19/2016
10.3.2a ^b	Pinnacle West APS	<u>First Amendment to the Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016)</u>	10.3.2a to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/24/2017
10.3.2b ^b	Pinnacle West APS	<u>Second Amendment to the Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016)</u>	10.3.2b to Pinnacle West/APS 2017 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/23/2018
10.4.1 ^b	Pinnacle West APS	<u>Letter Agreement dated June 17, 2008 between Pinnacle West/APS and James R. Hatfield</u>	10.1 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/7/2008
10.4.2 ^b	APS	<u>Retention Agreement dated December 19, 2008 between APS and Robert Bement</u>		
10.4.3 ^b	APS	<u>Discretionary Credit Award Agreement dated October 20, 2014 between APS and Robert Bement</u>		
10.5.1 ^{bd}	Pinnacle West APS	<u>Key Executive Employment and Severance Agreement between Pinnacle West and certain executive officers of Pinnacle West and its subsidiaries</u>	10.77bd to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/13/2006

10.5.1a ^{bd}	Pinnacle West APS	<u>Form of Amended and Restated Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries</u>	10.4 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473	11/6/2007
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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.5.2 ^{bd}	Pinnacle West APS	<u>Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries</u>	10.3 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473	11/6/2007
10.5.3 ^{bd}	Pinnacle West APS	<u>Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries</u>	10.5.3 to Pinnacle West/APS 2009 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/19/2010
10.5.4 ^{bd}	Pinnacle West APS	<u>Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries</u>	10.5.4 to Pinnacle West/APS 2012 Form 10-K, File Nos. 1-8962 and 1-4473	2/22/2013
10.6.1 ^b	Pinnacle West	<u>Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	Appendix B to the Proxy Statement for Pinnacle West's 2007 Annual Meeting of Shareholders, File No. 1-8962	4/20/2007
10.6.1a ^b	Pinnacle West	<u>First Amendment to the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.2 to Pinnacle West/APS April 18, 2007 Form 8-K Report, File No. 1-8962	4/20/2007
10.6.1b ^{bd}	Pinnacle West APS	<u>Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.3 to Pinnacle West/APS March 31, 2009 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/5/2009
10.6.1c ^{bd}	Pinnacle West	<u>Form of Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.1 to Pinnacle West/APS June 30, 2010 Form 10-Q Report, File No. 1-8962	8/3/2010
10.6.1d ^{bd}	Pinnacle West	<u>Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.2 to Pinnacle West/APS June 30, 2010 Form 10-Q Report, File No. 1-8962	8/3/2010
10.6.1e ^{bd}	Pinnacle West	<u>Form of Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.4 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962	4/29/2011
10.6.1f ^{bd}	Pinnacle West	<u>Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan</u>	10.5 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962	4/29/2011
10.6.1g ^{bd}				4/29/2011

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	Pinnacle West	<u>Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan (Supplemental 2010 Award)</u>	10.6 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962	
10.6.2 ^b	Pinnacle West	<u>Description of Annual Stock Grants to Non-Employee Directors</u>	10.1 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File No. 1-8962	11/6/2007
10.6.3 ^b	Pinnacle West	<u>Description of Annual Stock Grants to Non-Employee Directors</u>	10.2 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File No. 1-8962	8/7/2008
10.6.4 ^{bd}	Pinnacle West APS	<u>Summary of 2019 Variable Incentive Plan and Officer Variable Incentive Plan</u>		

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.6.5	Pinnacle West	<u>Description of Restricted Stock Unit Grant to Donald E. Brandt</u>	Pinnacle West/APS December 24, 2012 Form 8-K Report, File No. 1-8962	12/26/2012
10.6.6 ^b	Pinnacle West APS	<u>Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	Appendix A to the Proxy Statement for Pinnacle West's 2012 Annual Meeting of Shareholders, File No. 1-8962	3/29/2012
10.6.6a ^{bd}	Pinnacle West	<u>Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.1 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/3/2012
10.6.6b ^{bd}	Pinnacle West	<u>Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.2 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/3/2012
10.6.6c ^{bd}	Pinnacle West	<u>Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.6.8c to Pinnacle West/APS 2013 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/21/2014
10.6.6d ^{bd}	Pinnacle West	<u>Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.6.8d to Pinnacle West/APS 2013 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/21/2014
10.6.6e ^{bd}	Pinnacle West	<u>Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.6.6e to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/19/2016
10.6.6f ^{bd}	Pinnacle West	<u>Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.6.6f to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/24/2017
10.6.6g ^{bd}	Pinnacle West	<u>Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	10.6.6g to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/24/2017
10.6.6h ^{bd}	Pinnacle West	<u>Master Amendment to Performance Share Agreements</u>	10.3 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/3/2012
10.6.6i ^{bd}	Pinnacle West	<u>Master Amendment to Restricted Stock Unit Agreements</u>	10.4 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962	5/3/2012

and 1-4473

10.6.6j ^{bd}	Pinnacle West	<u>Performance Cash Award Agreement, dated May 10, 2017, between Pinnacle West and Donald E. Brandt</u>	10.1 to Pinnacle West/APS June 30, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/2/2017
10.6.6k ^{bd}	Pinnacle West	<u>First Amendment to the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan</u>	Appendix A to the Proxy Statement for Pinnacle West's 2017 Annual Meeting of Shareholders, File No. 1-8962	3/31/2017
10.7.1	Pinnacle West APS	Indenture of Lease with Navajo Tribe of Indians, Four Corners Plant	5.01 to APS's Form S-7 Registration Statement, File No. 2-59644	9/1/1977

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.7.1a	Pinnacle West APS	Supplemental and Additional Indenture of Lease, including amendments and supplements to original lease with Navajo Tribe of Indians, Four Corners Plant	5.02 to APS's Form S-7 Registration Statement, File No. 2-59644	9/1/1977
10.7.1b	Pinnacle West APS	Amendment and Supplement No. 1 to Supplemental and Additional Indenture of Lease Four Corners, dated April 25, 1985	10.36 to Pinnacle West's Registration Statement on Form 8-B Report, File No. 1-89	7/25/1985
10.7.1c	Pinnacle West APS	<u>Amendment and Supplement No. 2 to Supplemental and Additional Indenture of Lease with the Navajo Nation dated March 7, 2011</u>	10.1 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File Nos. 1-8962 and 1-4473	4/29/2011
10.7.1d	Pinnacle West APS	<u>Amendment and Supplement No. 3 to Supplemental and Additional Indenture of Lease with the Navajo Nation dated March 7, 2011</u>	10.2 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File Nos. 1-8962 and 1-4473	4/29/2011
10.7.2	Pinnacle West APS	Application and Grant of multi-party rights-of-way and easements, Four Corners Plant Site	5.04 to APS's Form S-7 Registration Statement, File No. 2-59644	9/1/1977
10.7.2a	Pinnacle West APS	Application and Amendment No. 1 to Grant of multi-party rights-of-way and easements, Four Corners Site dated April 25, 1985	10.37 to Pinnacle West's Registration Statement on Form 8-B, File No. 1-8962	7/25/1985
10.7.3	Pinnacle West APS	Application and Grant of APS rights- of-way and easements, Four Corners Site	5.05 to APS's Form S-7 Registration Statement, File No. 2-59644	9/1/1977
10.7.3a	Pinnacle West APS	Application and Amendment No. 1 to Grant of APS rights-of-way and easements, Four Corners Site dated April 25, 1985	10.38 to Pinnacle West's Registration Statement on Form 8-B, File No. 1-8962	7/25/1985
10.7.4	Pinnacle West APS	<u>Four Corners Project Co-Tenancy Agreement, conformed copy up through and including Amendment No. 11, dated June 30, 2018, among APS, Public Service Company of New Mexico, SRP, Tucson Electric Power Company and Navajo Transitional Energy Company, LLC</u>	10.7.4c to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018
10.8.1	Pinnacle West APS	Indenture of Lease, Navajo Units 1, 2, and 3	5(g) to APS's Form S-7 Registration Statement, File No. 2-36505	3/23/1970
10.8.2	Pinnacle West	Application of Grant of rights-of-way and easements, Navajo Plant	5(h) to APS Form S-7 Registration Statement, File	3/23/1970

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APS

No. 2-36505

10.8.3	Pinnacle West APS	Water Service Contract Assignment with the United States Department of Interior, Bureau of Reclamation, Navajo Plant	5(1) to APS's Form S-7 Registration Statement, File No. 2-394442	3/16/1971
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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.8.4	Pinnacle West APS	<u>Navajo Project Co-Tenancy Agreement dated as of March 23, 1976, and Supplement No. 1 thereto dated as of October 18, 1976, Amendment No. 1 dated as of July 5, 1988, and Amendment No. 2 dated as of June 14, 1996; Amendment No. 3 dated as of February 11, 1997; Amendment No. 4 dated as of January 21, 1997; Amendment No. 5 dated as of January 23, 1998; Amendment No. 6 dated as of July 31, 1998</u>	10.107 to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/13/2006
10.8.5	Pinnacle West APS	<u>Navajo Project Participation Agreement dated as of September 30, 1969, and Amendment and Supplement No. 1 dated as of January 16, 1970, and Coordinating Committee Agreement No. 1 dated as of September 30, 1971</u>	10.108 to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/13/2006
10.9.1	Pinnacle West APS	ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles, and amendments 1-12 thereto	10. 1 to APS's 1988 Form 10-K Report, File No. 1-4473	3/8/1989
10.9.1a	Pinnacle West APS	Amendment No. 13, dated as of April 22, 1991, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles	10.1 to APS's March 31, 1991 Form 10-Q Report, File No. 1-4473	5/15/1991
10.9.1b	Pinnacle West APS	<u>Amendment No. 14 to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles</u>	99.1 to Pinnacle West's June 30, 2000 Form 10-Q Report, File No. 1-8962	8/14/2000
10.9.1c	Pinnacle West APS	<u>Amendment No. 15, dated November 29, 2010, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles</u>	10.9.1c to Pinnacle West/APS 2010 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/18/2011

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.9.1d	Pinnacle West APS	<u>Amendment No. 16, dated April 28, 2014, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles</u>	10.2 to Pinnacle West/APS March 31, 2014 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/2/2014
10.10.1	Pinnacle West APS	Asset Purchase and Power Exchange Agreement dated September 21, 1990 between APS and PacifiCorp, as amended as of October 11, 1990 and as of July 18, 1991	10.1 to APS's June 30, 1991 Form 10-Q Report, File No. 1-4473	8/8/1991
10.10.2	Pinnacle West APS	Long-Term Power Transaction Agreement dated September 21, 1990 between APS and PacifiCorp, as amended as of October 11, 1990, and as of July 8, 1991	10.2 to APS's June 30, 1991 Form 10-Q Report, File No. 1-4473	8/8/1991
10.10.2a	Pinnacle West APS	<u>Amendment No. 1 dated April 5, 1995 to the Long-Term Power Transaction Agreement and Asset Purchase and Power Exchange Agreement between PacifiCorp and APS</u>	10.3 to APS's 1995 Form 10-K Report, File No. 1-4473	3/29/1996
10.10.3	Pinnacle West APS	<u>Restated Transmission Agreement between PacifiCorp and APS dated April 5, 1995</u>	10.4 to APS's 1995 Form 10-K Report, File No. 1-4473	3/29/1996
10.10.4	Pinnacle West APS	<u>Contract among PacifiCorp, APS and DOE Western Area Power Administration, Salt Lake Area Integrated Projects for Firm Transmission Service dated May 5, 1995</u>	10.5 to APS's 1995 Form 10-K Report, File No. 1-4473	3/29/1996
10.10.5	Pinnacle West APS	<u>Reciprocal Transmission Service Agreement between APS and PacifiCorp dated as of March 2, 1994</u>	10.6 to APS's 1995 Form 10-K Report, File No. 1-4473	3/29/1996
10.11.1	Pinnacle West	<u>Term Loan Agreement dated as of December 21, 2018 among Pinnacle West, as Borrower, KeyBank National Association, as Agent, PNC Bank, National Association and Wells Fargo Bank, National Association, as Co-Syndication Agents and such institutions compromising the lenders party thereto</u>		
10.11.2	Pinnacle West	<u>Five-Year Credit Agreement dated as of July 12, 2018, among Pinnacle West, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto</u>	10.3 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.11.3	Pinnacle West	<u>364-day Credit Agreement dated as of June 28, 2018, among Pinnacle West, as Borrower, MUFG Bank, Ltd., as Agent and Issuing Bank, JPMorgan Chase Bank, N.A. and Bank of America, N.A., as Co-Syndication Agent</u>	10.1 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018
10.11.4	Pinnacle West APS	<u>Five-Year Credit Agreement dated as of June 29, 2017 among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto</u>	10.2 to Pinnacle West/APS June 30, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2017
10.11.4a	Pinnacle West APS	<u>Amendment No. 1, dated July 13, 2018, to Five-Year Credit Agreement dated as of June 29, 2017, among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto</u>	10.11.4a to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018
10.11.5	Pinnacle West APS	<u>Five-Year Credit Agreement dated as of July 12, 2018 among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto</u>	10.4 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018
10.12.1 ^c	Pinnacle West APS	Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee	4.3 to APS's Form 18 Registration Statement, File No. 33-9480	10/24/1986
10.12.1a ^c	Pinnacle West APS	Amendment No. 1, dated as of November 1, 1986, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee	10.5 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1 on December 3, 1986 Form 8, File No. 1-4473	12/4/1986
10.12.1b ^c	Pinnacle West APS	Amendment No. 2 dated as of June 1, 1987 to Facility Lease dated as of August 1, 1986 between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee	10.3 to APS's 1988 Form 10-K Report, File No. 1-4473	3/8/1989
10.12.1c ^c	Pinnacle West APS	Amendment No. 3, dated as of March 17, 1993, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association,	10.3 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993

successor to State Street Bank and Trust
Company, as successor to The First National
Bank of Boston, as Lessor, and APS, as Lessee

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.12.1d ^c	Pinnacle West APS	<u>Amendment No. 4, dated as of September 30, 2015, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, 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 Emerson Finance LLC, as Lessor, and APS, as Lessee</u>	10.2 to Pinnacle West/APS September 30, 2015 Form 10-Q Report, File Nos. 1-8962 and 1-4473	10/30/2015
10.12.1e ^c	Pinnacle West APS	<u>Amendment No. 3, dated as of September 30, 2015, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, 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 Security Pacific Capital Leasing Corporation, as Lessor, and APS, as Lessee</u>	10.3 to Pinnacle West/APS September 30, 2015 Form 10-Q Report, File Nos. 1-8962 and 1-4473	10/30/2015
10.12.2	Pinnacle West APS	Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee	10.1 to APS's November 18, 1986 Form 8-K Report, File No. 1-4473	1/20/1987
10.12.2a	Pinnacle West APS	Amendment No. 1, dated as of August 1, 1987, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee	4.13 to APS's Form 18 Registration Statement No. 33-9480 by means of August 1, 1987 Form 8-K Report, File No. 1-4473	8/24/1987
10.12.2b	Pinnacle West APS	Amendment No. 2, dated as of March 17, 1993, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee	10.4 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
10.12.2c	Pinnacle West APS	<u>Amendment No. 3, dated July 10, 2014, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to the First National Bank of Boston, as Lessor, and APS, as Lessee</u>	10.2 to Pinnacle West/APS June 30, 2014 Form 10-Q Report, File Nos. 1-8962 and 1-4473	7/31/2014

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.13.1	Pinnacle West APS	<u>Agreement between Pinnacle West Energy Corporation and APS for Transportation and Treatment of Effluent by and between Pinnacle West Energy Corporation and APS dated as of the 10th day of April, 2001</u>	10.102 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/16/2005
10.13.2	Pinnacle West APS	<u>Agreement for the Transfer and Use of Wastewater and Effluent by and between APS, SRP and PWE dated June 1, 2001</u>	10.103 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/16/2005
10.13.3	Pinnacle West APS	<u>Agreement for the Sale and Purchase of Wastewater Effluent dated November 13, 2000, by and between the City of Tolleson, Arizona, APS and SRP</u>	10.104 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/16/2005
10.13.4	Pinnacle West APS	<u>Operating Agreement for the Co-Ownership of Wastewater Effluent dated November 16, 2000 by and between APS and SRP</u>	10.105 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473	3/16/2005
10.13.5	Pinnacle West APS	<u>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 SRP</u>	10.1 to Pinnacle West/APS March 31, 2010 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/6/2010
10.14.1	Pinnacle West APS	Contract, dated July 21, 1984, with DOE providing for the disposal of nuclear fuel and/or high-level radioactive waste, ANPP	10.31 to Pinnacle West's Form S-14 Registration Statement, File No. 2-96386	3/13/1985
10.15.1	Pinnacle West APS	<u>Territorial Agreement between APS and SRP</u>	10.1 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473	5/15/1998
10.15.2	Pinnacle West APS	<u>Power Coordination Agreement between APS and SRP</u>	10.2 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473	5/15/1998
10.15.3	Pinnacle West APS	<u>Memorandum of Agreement between APS and SRP</u>	10.3 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473	5/15/1998
10.15.3a	Pinnacle West APS	<u>Addendum to Memorandum of Agreement between APS and SRP dated as of May 19, 1998</u>	10.2 to APS's May 19, 1998 Form 8-K Report, File No. 1-4473	6/26/1998
10.16	Pinnacle West APS	<u>Purchase and Sale Agreement dated November 8, 2010 by and between SCE and APS</u>	10.1 to Pinnacle West/APS November 8, 2010 Form 8-K Report, File Nos. 1-8962 and	11/8/2010

1-4473

10.17	Pinnacle West APS	<u>Proposed Settlement Agreement dated January 6, 2012 by and among APS and certain parties to its retail rate case (approved by ACC Order No. 73183)</u>	10.17 to Pinnacle West/APS 2011 Form 10-K Report, File Nos. 1-8962 and 1-4473	2/24/2012
10.18	Pinnacle West APS	<u>Proposed Settlement Agreement dated March 27, 2017 by and among APS and certain parties to its retail rate case (approved by ACC Order No. 76295)</u>	10.1 to Pinnacle West/APS March 31, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473	5/2/2017

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
10.19	Pinnacle West	<u>Purchase and Sale Agreement, dated June 29, 2018, by and between Navajo Transitional Energy Company, LLC and 4CA</u>	10.2 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/3/2018
21.1	Pinnacle West	<u>Subsidiaries of Pinnacle West</u>		
23.1	Pinnacle West	<u>Consent of Deloitte & Touche LLP</u>		
23.2	APS	<u>Consent of Deloitte & Touche LLP</u>		
31.1	Pinnacle West	<u>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</u>		
31.2	Pinnacle West	<u>Certificate of James R. Hatfield, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended</u>		
31.3	APS	<u>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</u>		
31.4	APS	<u>Certificate of James R. Hatfield, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended</u>		
32.1 ^e	Pinnacle West	<u>Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>		
32.2 ^e	APS	<u>Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>		
99.1	Pinnacle West APS	Collateral Trust Indenture among PVGS II Funding Corp., Inc., APS and Chemical Bank, as Trustee	4.2 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.1a	Pinnacle West APS	Supplemental Indenture to Collateral Trust Indenture among PVGS II Funding Corp., Inc., APS and Chemical Bank, as Trustee	4.3 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.2 ^c				11/9/1992

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Pinnacle West APS Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., Bank of America National Trust and Savings Association, State Street Bank No. 1-4473 and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein 28.1 to APS's September 30, 1992 Form 10-Q Report, File

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
99.2a ^c	Pinnacle West APS	Amendment No. 1 dated as of November 1, 1986, to Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., Bank of America National Trust and Savings Association, State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein	10.8 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1, on December 3, 1986 Form 8, File No. 1-4473	12/4/1986
99.2b ^c	Pinnacle West APS	Amendment No. 2, dated as of March 17, 1993, to Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., PVGS II Funding Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein	28.4 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.3 ^c	Pinnacle West APS	Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee	4.5 to APS's Form 18 Registration Statement, File No. 33-9480	10/24/1986
99.3a ^c	Pinnacle West APS	Supplemental Indenture No. 1, dated as of November 1, 1986 to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee	10.6 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1 on December 3, 1986 Form 8, File No. 1-4473	12/4/1986
99.3b ^c	Pinnacle West APS	Supplemental Indenture No. 2 to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Lease Indenture Trustee	4.4 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.4 ^c	Pinnacle West APS	Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee	28.3 to APS's Form 18 Registration Statement, File No. 33-9480	10/24/1986

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
99.4a ^c	Pinnacle West APS	Amendment No. 1, dated as of November 1, 1986, to Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee	10.10 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1 on December 3, 1986 Form 8, File No. 1-4473	12/4/1986
99.4b ^c	Pinnacle West APS	Amendment No. 2, dated as of March 17, 1993, to Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee	28.6 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.5	Pinnacle West APS	Participation Agreement, dated as of December 15, 1986, among PVGS Funding Report Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee under a Trust Indenture, APS, and the Owner Participant named therein	28.2 to APS's September 30, 1992 Form 10-Q Report, File No. 1-4473	11/9/1992
99.5a	Pinnacle West APS	Amendment No. 1, dated as of August 1, 1987, to Participation Agreement, dated as of December 15, 1986, among PVGS Funding Corp., Inc. as Funding Corporation, State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, Chemical Bank, as Indenture Trustee, APS, and the Owner Participant named therein	28.20 to APS's Form 18 Registration Statement No. 33-9480 by means of a November 6, 1986 Form 8-K Report, File No. 1-4473	8/10/1987
99.5b	Pinnacle West APS	Amendment No. 2, dated as of March 17, 1993, to Participation Agreement, dated as of December 15, 1986, among PVGS Funding Corp., Inc., PVGS II Funding Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Owner Participant named therein	28.5 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.6	Pinnacle West APS	Trust Indenture, Mortgage Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee	10.2 to APS's November 18, 1986 Form 10-K Report, File No. 1-4473	1/20/1987

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
99.6a	Pinnacle West APS	Supplemental Indenture No. 1, dated as of August 1, 1987, to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee	4.13 to APS's Form 18 Registration Statement No. 33-9480 by means of August 1, 1987 Form 8-K Report, File No. 1-4473	8/24/1987
99.6b	Pinnacle West APS	Supplemental Indenture No. 2 to Trust Indenture Mortgage, Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Lease Indenture Trustee	4.5 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.7	Pinnacle West APS	Assignment, Assumption and Further Agreement, dated as of December 15, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee	10.5 to APS's November 18, 1986 Form 8-K Report, File No. 1-4473	1/20/1987
99.7a	Pinnacle West APS	Amendment No. 1, dated as of March 17, 1993, to Assignment, Assumption and Further Agreement, dated as of December 15, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee	28.7 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.8 ^c	Pinnacle West APS	Indemnity Agreement dated as of March 17, 1993 by APS	28.3 to APS's 1992 Form 10-K Report, File No. 1-4473	3/30/1993
99.9	Pinnacle West APS	Extension Letter, dated as of August 13, 1987, from the signatories of the Participation Agreement to Chemical Bank	28.20 to APS's Form 18 Registration Statement No. 33-9480 by means of a November 6, 1986 Form 8-K Report, File No. 1-4473	8/10/1987
99.10	Pinnacle West APS	<u>ACC Order, Decision No. 61969, dated September 29, 1999, including the Retail Electric Competition Rules</u>	10.2 to APS's September 30, 1999 Form 10-Q Report, File No. 1-4473	11/15/1999
99.11	Pinnacle West	<u>Purchase Agreement by and among Pinnacle West Energy Corporation and GenWest, L.L.C. and Nevada Power Company, dated June 21, 2005</u>	99.5 to Pinnacle West/APS June 30, 2005 Form 10-Q Report, File Nos. 1-8962 and 1-4473	8/9/2005

101.SCH West Pinnacle
APS XBRL Taxonomy Extension Schema Document

101.CAL West Pinnacle
APS XBRL Taxonomy Extension Calculation
Linkbase Document

101.LAB West Pinnacle
APS XBRL Taxonomy Extension Label Linkbase
Document

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Exhibit No.	Registrant(s)	Description	Previously Filed as Exhibit: a	Date Filed
101.PRE	Pinnacle West APS	XBRL Taxonomy Extension Presentation Linkbase Document		
101.DEF	Pinnacle West APS	XBRL Taxonomy Definition Linkbase Document		

^aReports filed under File No. 1-4473 and 1-8962 were filed in the office of the Securities and Exchange Commission located in Washington, D.C.

^bManagement contract or compensatory plan or arrangement to be filed as an exhibit pursuant to Item 15(b) of Form 10-K.

^cAn additional document, substantially identical in all material respects to this Exhibit, has been entered into, relating to an additional Equity Participant. Although such additional document may differ in other respects (such as dollar amounts, percentages, tax indemnity matters, and dates of execution), there are no material details in which such document differs from this Exhibit.

^dAdditional agreements, substantially identical in all material respects to this Exhibit have been entered into with additional persons. Although such additional documents may differ in other respects (such as dollar amounts and dates of execution), there are no material details in which such agreements differ from this Exhibit.

^eFurnished herewith as an Exhibit.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PINNACLE WEST CAPITAL CORPORATION
(Registrant)

Date: February 22, 2019 /s/ Donald E. Brandt
(Donald E. Brandt, Chairman of
the Board of Directors, President and
Chief Executive Officer)

Power of Attorney

We, the undersigned directors and executive officers of Pinnacle West Capital Corporation, hereby severally appoint James R. Hatfield and Robert E. Smith, and each of them, our true and lawful attorneys with full power to them and each of them to sign for us, and in our names in the capacities indicated below, any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Donald E. Brandt (Donald E. Brandt, Chairman of the Board of Directors, President and Chief Executive Officer)	Principal Executive Officer and Director	February 22, 2019
/s/ James R. Hatfield (James R. Hatfield, Executive Vice President and Chief Financial Officer)	Principal Financial Officer	February 22, 2019
/s/ Denise R. Danner (Denise R. Danner, Vice President, Controller and Chief Accounting Officer)	Principal Accounting Officer	February 22, 2019

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/s/ Denis A. Cortese, M.D. Director February 22, 2019
(Denis A. Cortese, M.D.)

/s/ Richard P. Fox Director February 22, 2019
(Richard P. Fox)

/s/ Michael L. Gallagher Director February 22, 2019
(Michael L. Gallagher)

/s/ Dale E. Klein, Ph.D. Director February 22, 2019
(Dale E. Klein, Ph.D.)

/s/ Humberto S. Lopez Director February 22, 2019
(Humberto S. Lopez)

/s/ Kathryn L. Munro Director February 22, 2019
(Kathryn L. Munro)

/s/ Bruce J. Nordstrom Director February 22, 2019
(Bruce J. Nordstrom)

/s/ Paula J. Sims Director February 22, 2019
(Paula J. Sims)

/s/ James E. Trevathan Director February 22, 2019
(James E. Trevathan)

/s/ David P. Wagener Director February 22, 2019
(David P. Wagener)

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ARIZONA PUBLIC SERVICE COMPANY
(Registrant)

Date: February 22, 2019 /s/ Donald E. Brandt
(Donald E. Brandt, Chairman of
the Board of Directors and Chief
Executive Officer)

Power of Attorney

We, the undersigned directors and executive officers of Arizona Public Service Company, hereby severally appoint James R. Hatfield and Robert E. Smith, and each of them, our true and lawful attorneys with full power to them and each of them to sign for us, and in our names in the capacities indicated below, any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Donald E. Brandt (Donald E. Brandt, Chairman of the Board of Directors and Chief Executive Officer)	Principal Executive Officer and Director	February 22, 2019
/s/ James R. Hatfield (James R. Hatfield, Executive Vice President and Chief Financial Officer)	Principal Financial Officer	February 22, 2019
/s/ Denise R. Danner (Denise R. Danner, Vice President, Controller and Chief Accounting Officer)	Principal Accounting Officer	February 22, 2019

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/s/ Denis A. Cortese, M.D. Director February 22, 2019
(Denis A. Cortese, M.D.)

/s/ Richard P. Fox Director February 22, 2019
(Richard P. Fox)

/s/ Michael L. Gallagher Director February 22, 2019
(Michael L. Gallagher)

/s/ Dale E. Klein Director February 22, 2019
(Dale E. Klein, Ph.D.)

/s/ Humberto S. Lopez Director February 22, 2019
(Humberto S. Lopez)

/s/ Kathryn L. Munro Director February 22, 2019
(Kathryn L. Munro)

/s/ Bruce J. Nordstrom Director February 22, 2019
(Bruce J. Nordstrom)

/s/ Paula J. Sims Director February 22, 2019
(Paula J. Sims)

/s/ James E. Trevathan Director February 22, 2019
(James E. Trevathan)

/s/ David P. Wagener Director February 22, 2019
(David P. Wagener)