NEW APPLICATION

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BEFORE THE ARIZONA CORPORATION COMMISSION

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NOTICE OF INTENT TO INCREASE EQUITY INTEREST IN ARIZONA PUBLIC SERVICE COMPANY UNDER A.A.C. R14-2-803.	DOCKET NO. E-01345A-05-____ **NOTICE** E-01345A-05-0520

Pinnacle West Capital Corporation ("PNW") hereby provides the Arizona Corporation Commission ("Commission") with 120 days notice of its intent to increase its equity interest in Arizona Public Service Company ("APS" or "Company") by an amount in excess of $100 million during calendar 2005 and, if necessary to maintain the Company's financial integrity, in subsequent years. Such notice is required under the provisions of A.A.C. R14-2-803 ("Rule 803") as modified by Decision No. 58063 (November 3, 1992).

I. INTRODUCTION

Rule 803 requires notice to the Commission of "reorganizations" by a public utility holding company such as Pinnacle West. A "reorganization" includes the "acquisition or divestiture of a financial interest in an affiliate or a [Class A] utility." A.A.C. R14-2-801(5). APS is a Class A utility, and thus both it and PNW are subject to the provisions of Rule 803.

In Decision No. 58063, the Commission interpreted the aforementioned language to also include any increase or decrease of an existing "financial interest" in a utility even if the increase/decrease did not change the status of the utility as a wholly-owned subsidiary of the public utility holding company. But, Decision No. 58063 effectively exempted from Rule 803's notice requirement any increase or decrease in a financial interest in a utility that was less than the so-called "exempt amount," which in the case of PNW and APS is $100 million per year. Thus, and pursuant to such Decision, PNW has already invested an additional $100 million in APS during 2005.

II. THE NEED TO INCREASE APS EQUITY

Rating agencies determine credit ratings based on a variety of quantitative and qualitative factors. In performing their qualitative analysis, the rating agency is assessing the business risk of a company by reviewing measures such as operations, management, economic environment, power supply and regulatory risk. The rating agency then reviews both historical and projected financial metrics in light of its business risk. The agency is looking to see that the ratios stay within predetermined target ranges. Standard and Poor's ("S&P") publishes the target ranges, while Moody's informs a company if any of the ratios are not meeting the level they think is appropriate for the existing credit rating.

APS' credit ratings are currently in the "BBB" investment grade range (BBB by S&P and Baa1 by Moody's). In addition, both have been assigned a "stable" outlook, meaning the agencies do not foresee an increase or decrease in the current ratings in the near future, assuming continuation of existing factors. Up until late April of 2005, both agencies had APS on "negative" outlook, meaning a high probability they would be downgrading the ratings. The reasons for their concern were: (1) the need for a rate increase; and (2) the additional up-front cash demands that come with the massive customer growth that APS experiences. Customer growth is especially demanding on APS since the Company needs to acquire additional power sources to meet its load growth.

The key financial metric the rating agencies are focusing on today is the Funds from Operations ("FFO") to Debt, or the ratio of operational cash flow to debt. Operational cash flow is essentially earnings plus certain non-cash expenses such as depreciation and deferred taxes. This single metric captures several of the more traditional metrics such as debt ratio, debt service coverage ratio, etc. In the 2000 to 2002 time frame, this ratio was solidly in the BBB target range, or in the case of S&P, was actually in the single A target range. *See* the 2 graphs attached as Exhibits A and B. However, over the past several years the ratio has consistently trended downward and has recently crossed into the non-investment grade BB range. Even with the recent rate increase, the ratio will still be non-investment grade absent additional efforts to shore up APS' financial strength. In the Company's last rate case, there was testimony that a downgrade of the Company's debt could cost APS customers as much as a billion dollars in higher interest costs over the next ten years. Thus, and in order to maintain our current credit ratings, APS needs additional equity to relieve the immediate and longer-term pressure on its financial metrics.

III. SOURCES AND AMOUNTS OF NEW EQUITY FUNDING FOR APS

In May of 2005, PNW issued $250 million of common stock equity. One of the stated purposes for that issuance was to raise funds that would be infused as additional equity capital into APS to preserve the Company's financial integrity. As noted previously, some $100 million of that amount has already been invested in APS pursuant to the provisions of Decision No. 58063.

In addition, PNW recently announced the pending sale of its Silverhawk power plant in Nevada for a purchase price of over $200 million. PNW intends that the entire proceeds from the sale will be reinvested in APS.

IV. IMPACT OF HIGHER EQUITY RATIO ON APS

By year-end 2005, APS would like to increase its common equity by in excess of $450 million through the combination of infusions from PNW and retention of its earnings. With the immediate addition of equity capital and the decrease in debt as a percent of capital, the FFO to Debt ratio stabilizes in 2005, returning back into the BBB investment grade range for at least one of the ratings agencies (S&P) and heading in the right direction toward the Moody's standard. See the 2 graphs attached as Exhibits C and D.

As a result of the above actions, which reflect PNW management's commitment to reduce financial pressures on APS, both ratings agencies changed the outlook for APS from negative to stable. In their article dated April 27, 2005, Moody's states: "The change in outlook also reflects the company's [APS] demonstrated intent to improve its financial strength by financing a portion of its rising capital expenditures with equity." And on April 27, 2005 S&P wrote "Both the equity issuance and the potential sale of Silverhawk were factored into S&P's action last month to revise the outlook on APS and PWCC's rating to stable from negative." Copies of both articles are attached as Exhibits E and F.

The beneficial impact of maintaining at least minimum investment grade debt ratings has been discussed on several occasions, most recently in the Company's last rate case, but also in its last two financing proceedings.[1] That impact can be measured in both lower interest rates and in greater access to capital markets during tight credit periods. Maintaining APS' investment grade credit quality and its commensurate access to the capital markets at reasonable costs is essential for our customers and the state.

In addition to higher credit quality, more equity investment will mean less debt and less interest than will otherwise be the case. For every $100 million not borrowed, APS will save $50 million in interest over a ten-year period, even at a historically-low interest rate of just 5%. Assuming a coverage ratio of 3.0 times, this means that for every dollar of saved interest cost, APS will need three less dollars of pre-tax earnings to maintain that coverage ratio.

V. STANDARD FOR REORGANIZATIONS AFFECTING A PUBLIC UTILITY

The test for whether a "reorganization" can be rejected by the Commission under Rule 803 is whether the "reorganization" would: (1) impair the financial status of the public utility; (2) prevent the public utility from attracting capital on fair and reasonable terms; or (3) impair the ability of the public utility to provide safe, reasonable and adequate service. The proposed increase in PNW's equity investment in APS clearly will not have (indeed, could not have) any of these negative impacts on APS. Rather it will enhance the financial status of APS, permit APS to attract capital on terms that are more favorable, and is essential to the Company's ability to provide safe, reasonable and reliable service.

VI. CONCLUSION

APS serves one of the fastest growing regions of the country. Its outside capital needs are substantial and will continue to be substantial for the foreseeable future. Therefore, the cost to APS customers of degraded credit quality is similarly substantial, in terms of higher interest rates and potential inability to access needed capital as well as in threats to service quality. PNW believes that increasing its equity stake in APS is an essential element of maintaining APS as an investment-grade utility. It asks that the Commission permit this Notice to expire after 120 days without action by the Commission.

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[1] *See* Docket Nos. E-01345A-02-0707 and E-01345A-02-0840, which resulted in Decision Nos. 65796 (April 4, 2003) and 65434 (December 3, 2002), respectively.

RESPECTFULLY SUBMITTED this 20th day of July, 2005.

Thomas L. Mumaw

Thomas L. Mumaw

Attorney for Pinnacle West Capital Corporation and Arizona Public Service Company

The original and 13 copies of the foregoing were filed this 20th day of July, 2005 with:

Docket Control
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1200 West Washington
Phoenix, AZ 85007.

Vicki DiCola

Vicki DiCola

Exhibit A
APS
Historical FFO/Debt
S&P

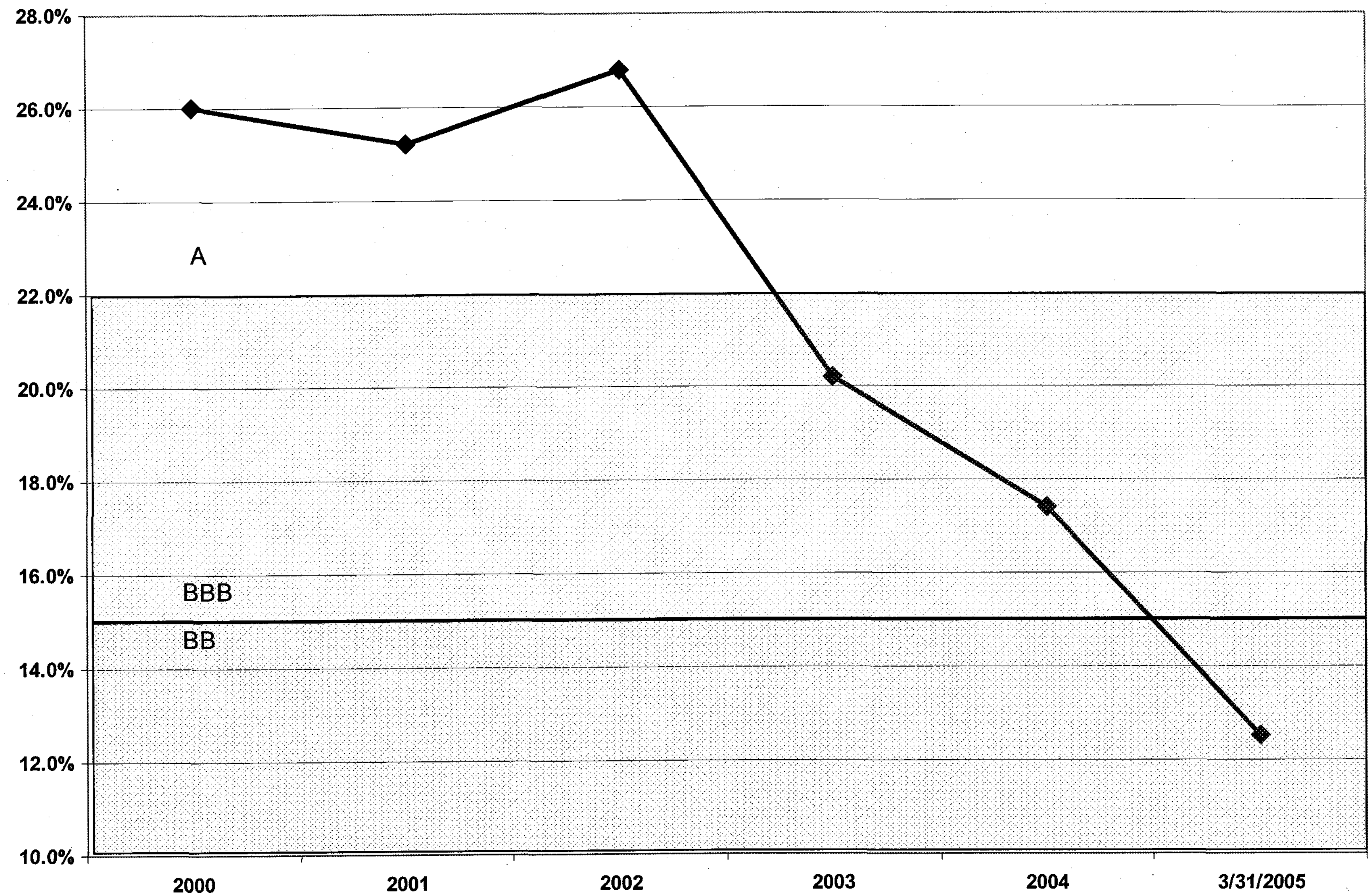

Exhibit B
APS
Historical FFO/Debt
Moody's

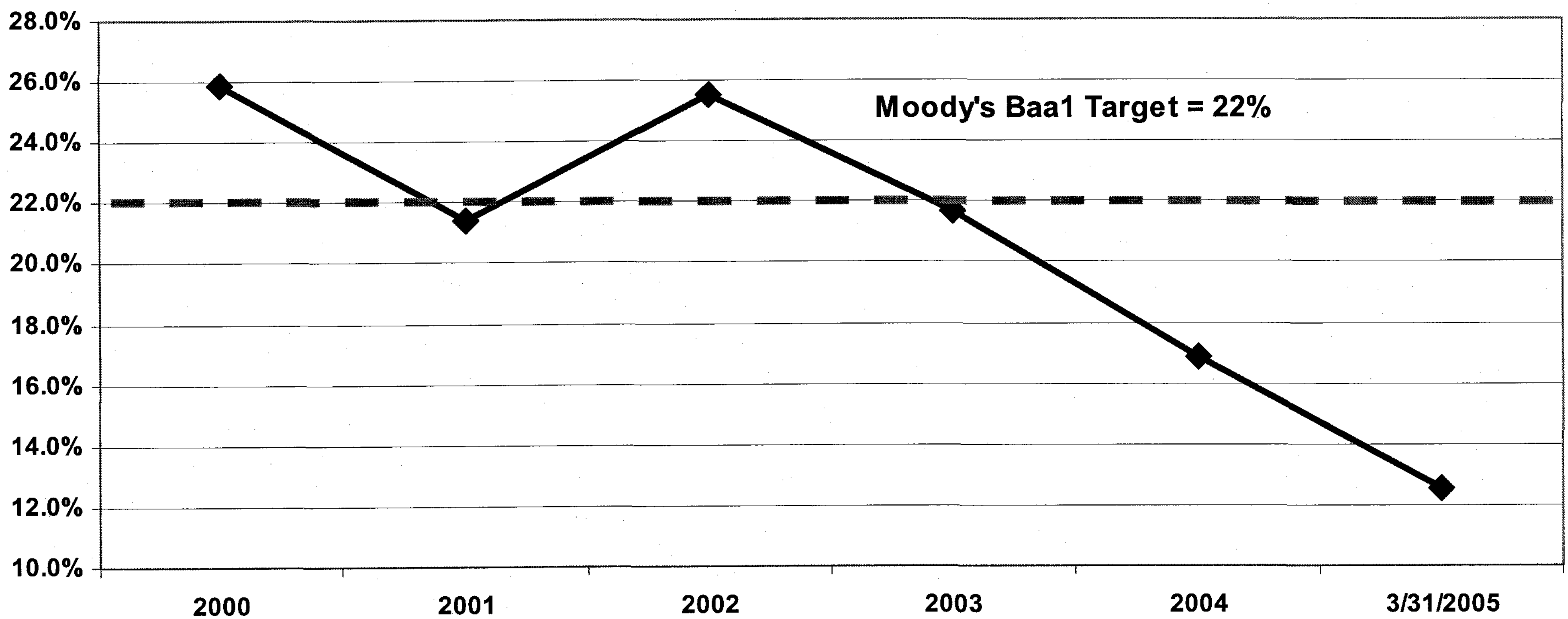

Exhibit C
APS
FFO/Debt with $450M Equity
S&P

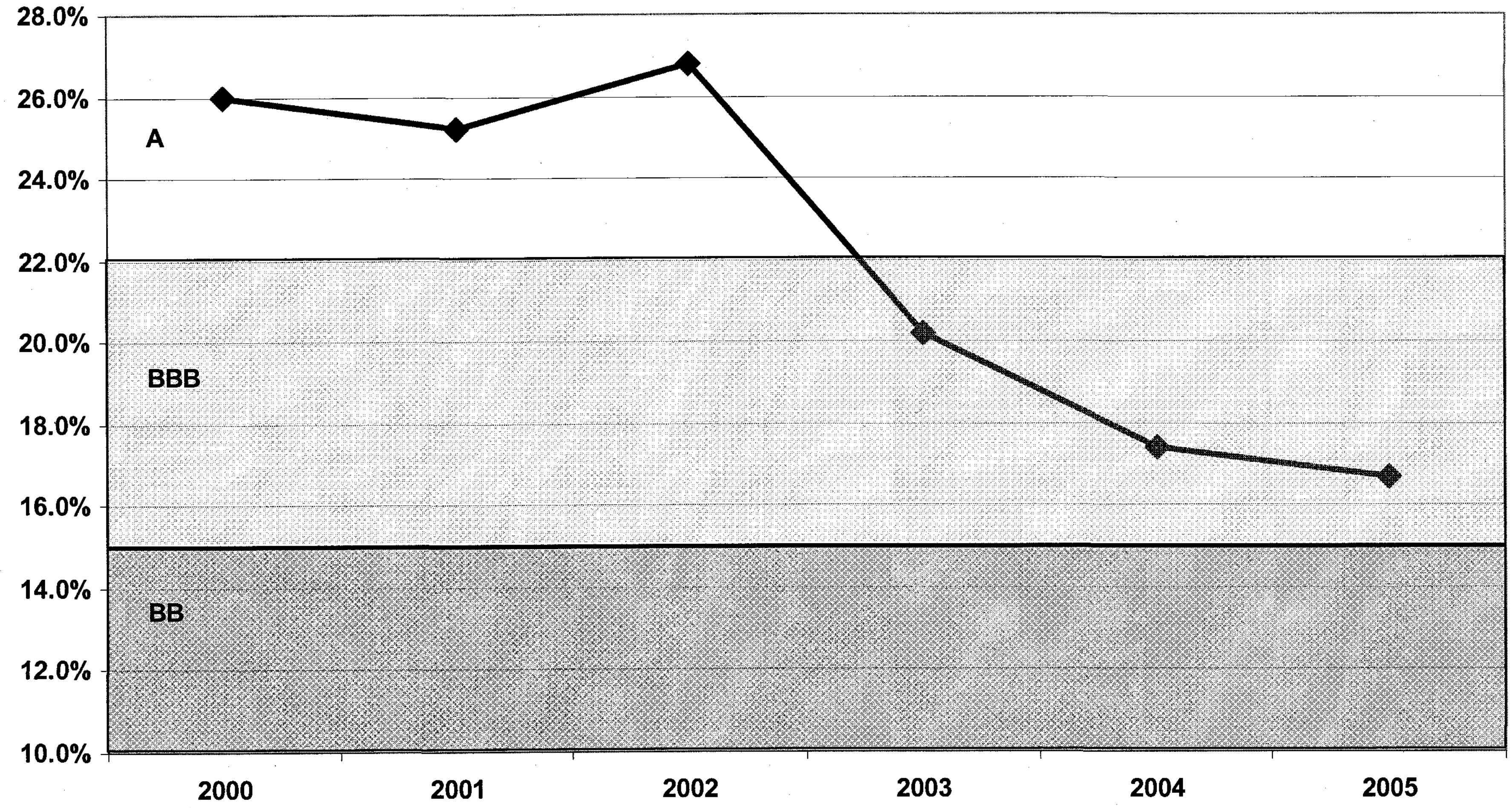

Exhibit D
APS
FFO/Debt with $450M Equity
Moody's

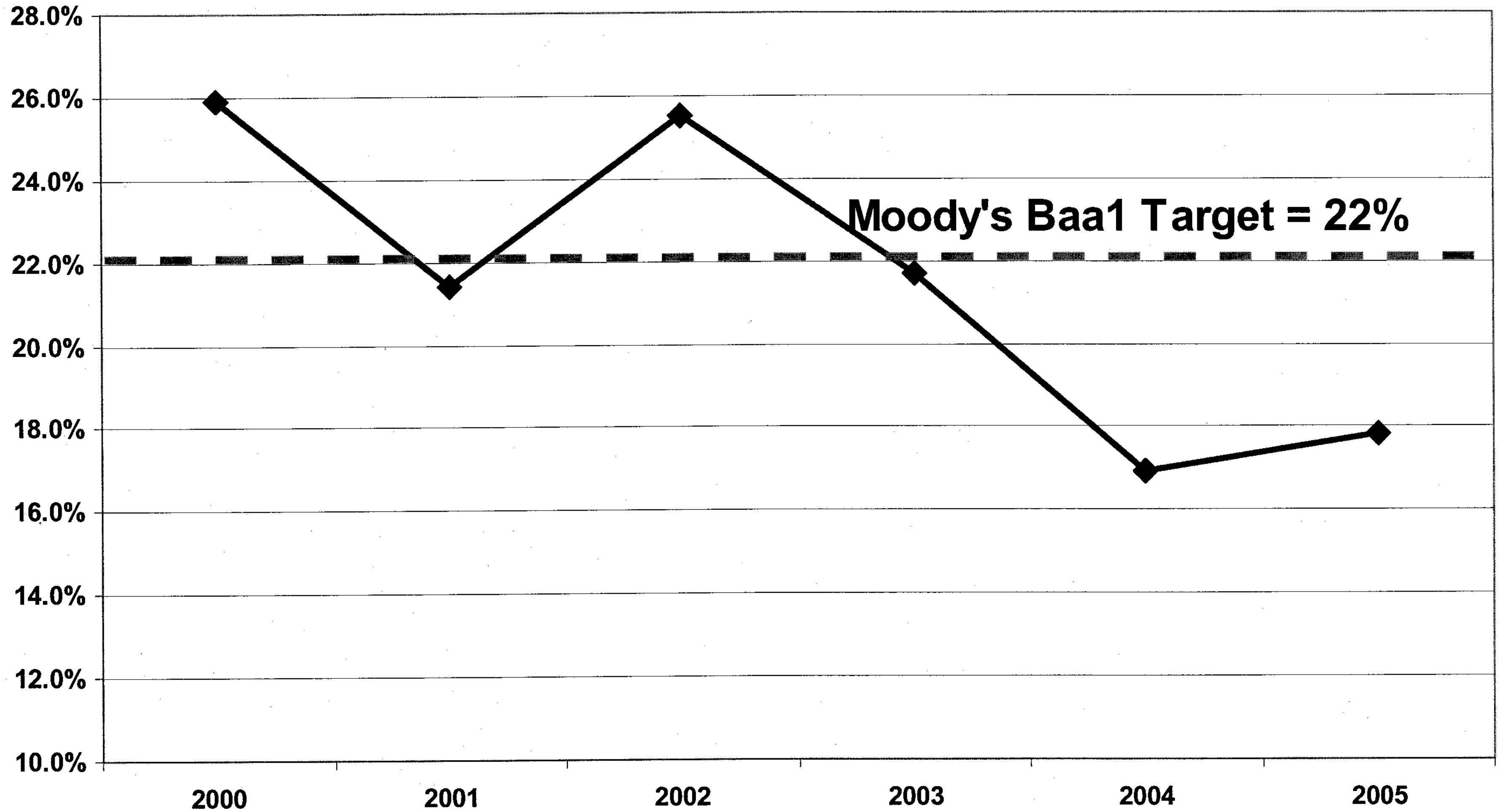

Exhibit E

STANDARD &POOR'S	RATINGSDIRECT

Return to Regular Format

Research:

BULLETIN: Common Stock Issuance And Planned Asset Sale Supportive Of APS And PWCC Ratings

Publication date: 27-Apr-2005
Primary Credit Analyst(s): Anne Selting, San Francisco (1) 415-371-5009; anne_selting@standardandpoors.com

SAN FRANCISCO (Standard & Poor's) April 27, 2005--Standard & Poor's Ratings Services said today that Pinnacle West Capital Corporation's (PWCC; BBB/Stable/A-2) plans to offer common stock to bolster the balance sheet of its utility, along with its expectation that it will sell its interest in a merchant power plant, is supportive of the current credit ratings.

The company expects to sell 5.3 million shares, along with an additional 795,000 shares to cover any over-allotments. The offering is expected to yield about $250 million in proceeds, which the company will use to make an equity investment into Arizona Public Service Co. (APS) to offset rising capital expenditures.

PWCC also announced that it expects that its 75% interest in Silverhawk, which is owned by a separate subsidiary, Pinnacle West Energy Corp., will be sold within the next year. The sale would end the PWCC's exposure to merchant generation. Management has committed that the proceeds from a sale of Silverhawk will also be injected into the utility.

Both the equity issuance and the potential sale of Silverhawk were factored into Standard & Poor's action last month to revise the outlook on APS and PWCC's ratings to stable from negative.

Exhibit F

Moody's Investors Service

Global Credit Research
Rating Action
27 APR 2005

Rating Action: Pinnacle West Capital Corporation

MOODY'S AFFIRMS THE DEBT RATINGS OF PINNACLE WEST (Sr. Uns. Baa2) AND ARIZONA PUBLIC SERVICE CO. (Sr. Uns. Baa1); OUTLOOK CHANGED TO STABLE FROM NEGATIVE

Approximately $4.0 Billion of Debt Securities Affected

New York, April 27, 2005 -- Moody's Investors Service affirmed the ratings of Pinnacle West Capital Corporation (Pinnacle: Baa2, senior unsecured) and its subsidiaries Arizona Public Service Company (APS: Baa1, senior unsecured) and Pinnacle West Energy Corporation (PWEC: Baa2, senior unsecured), and changed the rating outlook to stable from negative. In addition, Moody's upgraded the secured lease obligation bonds of PVNGS II Funding Corp., Inc. (PVNGS II) to Baa1 from Baa2. The rating outlook is stable for PVNGS II.

The revision of the rating outlook reflects the projected stabilization of cash flow metrics at both APS and Pinnacle following a recent rate case decision at APS, yesterday's announced equity offering at Pinnacle with expected proceeds of approximately $250 million, and the expected sale of Pinnacle's ownership interest in the Silverhawk generating facility. By 2006, the ratio of adjusted funds from operations (FFO) to total adjusted debt is projected to be about 20% for APS, which is above Moody's previous expectations. Pinnacle's FFO as a percentage of total adjusted debt is projected to be about 18% in 2006, a level which is also above Moody's previous expectations.

The change in outlook considers the near term rate clarity that has resulted from the conclusion of APS' rate case in March. Although the approved rate increase was less than half of the company's original request, the Arizona Corporation Commission (ACC) decision allowed for a 4.2% increase in retail rates and provided for the inclusion of 1,800 MW of PWEC held generating capacity in APS' rate base. The decision also incorporated an adjustment mechanism for the cost of fuel and purchased power that is expected to positively impact cash flow beginning in 2006.

The change in outlook also reflects the company's demonstrated intent to improve its financial strength by financing a portion of its rising capital expenditures with equity. The proceeds of Pinnacle's equity offering will be used to fund a portion of APS' 2005 capital expenditures, including the purchase of the Sundance plant. Proceeds of the expected Silverhawk sale will also be contributed as equity to APS.

The lease obligation bonds of PVNGS II are secured by payments from APS made in conjunction with its sale leaseback of a portion of the Palo Verde Unit 2 nuclear facility. The upgrade reflects the critical value of the Palo Verde facility in supplying the growing service territory of APS, and recognizes that in the unlikely event of a distress situation, recovery for the lease bonds would likely be similar to the recovery for senior unsecured debt of APS.

Ratings affirmed include:

Pinnacle West Capital Corporation:

- Issuer Rating, senior unsecured debt and syndicated bank credit facility; Baa2,

- Shelf registration for the issuance of senior and subordinate debt securities and preferred stock; (P)Baa2, (P)Baa3, and (P)Ba1 respectively,

- Short term rating for commercial paper; Prime-2.

Arizona Public Service Company:

- Issuer Rating, senior unsecured debt and syndicated bank credit facility; Baa1,

- Shelf registration for the issuance of senior or subordinate debt securities; (P)Baa1 and (P)Baa2 respectively.

- Short term rating for commercial paper; Prime-2.

Pinnacle West Energy Company (rating based upon the guarantee of Pinnacle):

- Senior unsecured debt; Baa2.

Rating upgraded:

- Senior secured lease obligation bonds of PVNGS II, upgraded to Baa1 from Baa2.

Headquartered in Phoenix Arizona, Pinnacle West Capital Corporation provides electric service to a substantial portion of the state of Arizona, sells energy-related products and services, and develops residential, commercial and industrial real estate. Pinnacle conducts its business through subsidiaries. Wholly owned subsidiary Arizona Public Service Company is its principal subsidiary.

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ownership interest in MCO of more than 5%, is posted annually on Moody's website at www.moodys.com under the heading "Shareholder Relations - Corporate Governance - Director and Shareholder Affiliation Policy."