

NEW APPLICATION



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BEFORE THE ARIZONA CORPORATION COMMISSION

2002 NOV -8 P 4: 12

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4 Commissioner
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6 Commissioner

Arizona Corporation Commission
DOCKETED

AZ CORP COMMISSION
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NOV 08 2002

E-01345A-02-0840

DOCKETED BY *CK*

7 IN THE MATTER OF THE EMERGENCY
8 APPLICATION OF ARIZONA PUBLIC
9 SERVICE COMPANY FOR A PARTIAL
10 WAIVER OF A.A.C. R 14-2-804(B)(1) AND (2)

DOCKET NO. E-01345A-02-_____
EMERGENCY APPLICATION

11 Arizona Public Service Company ("APS" or "Company") is making this
12 emergency request to address a deteriorating financial situation arising from the Arizona
13 Corporation Commission's ("Commission") dramatic "reversal of course" on divestiture
14 of generation assets by APS and the necessary integration of APS and Pinnacle West
15 Energy Corporation ("PWEC") generation as called for under the 1999 APS Settlement
16 Agreement and the Commission's Electric Competition Rules. The combination of
17 Decision No. 65154 (September 10, 2002) and the current tumultuous state of the nation's
18 credit markets for energy-related companies—described as "one of the worst times in
19 recent history to refinance debt"—has now triggered a series of events that if left
20 unchecked could lead to a financial crisis.

21 APS therefore requests, through this verified Application, an order from the
22 Commission granting, to the extent necessary, a partial waiver of A.A.C. R 14-2-
23 804(B)(1) and (2) ("Rule 804") to allow APS to make short-term advances to Pinnacle
24 West Capital Corporation ("Pinnacle West") in the form of an inter-affiliate line of credit
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1 or, alternatively, in the form of an APS guarantee of Pinnacle West's short-term debt.¹ In
2 either case, the partial waiver would be limited to a maximum aggregate principal amount
3 of \$125 million and for a maximum term of 364 days. APS further requests that this
4 Application be decided by the Commission on an emergency basis at its November 19,
5 2002 Open Meeting, and although no hearing is required by A.A.C. R14-2-806 ("Rule
6 806") for a waiver of Rule 804, the Company hereby waives any right it might otherwise
7 have to an evidentiary hearing on this request.

8 INTRODUCTION

9 On September 16, 2002, APS filed an application with the Commission (the
10 "Financing Application") requesting the Commission to allow APS to borrow up to \$500
11 million and to lend the proceeds to Pinnacle West Energy Corporation ("PWEC") or
12 Pinnacle West; to guarantee up to \$500 million of PWEC's or Pinnacle West's debt; or a
13 combination of both, not to exceed \$500 million in the aggregate. The loan and/or
14 guarantee would be used to refinance the debt incurred by Pinnacle West to fund the
15 construction of PWEC's generation assets. These assets were built at PWEC and funded
16 by Pinnacle West because of the Commission's Electric Competition Rules, the
17 Commission-imposed APS Code of Conduct, and the Commission-authorized and
18 approved 1999 Settlement Agreement. That they were built at all is a direct result of the
19 Company's obligation to serve its customers' needs for power—needs that were otherwise
20 unaddressed by the Electric Competition Rules but which could not be left unmet by the
21 Company.

22
23 ¹ To the extent APS does not take back any "bonds, notes or other evidences of indebtedness" under
24 the inter-affiliate loan scenario, the transaction is exempt from Rule 804(B)(2) under the provisions of
25 Decision No. 58063 (November 3, 1992). A Commission determination to that effect would have the same
26 practical effect as a waiver. Likewise, approval of the proposed transaction under Rule 804(C) would
address this emergency. APS has no preference as to how the Commission resolves the problem so long as
it is resolved in the time permitted by current circumstances.

1 Even at the time the Track A order was decided, the financial situation facing APS
2 and its affiliates reflected the following circumstances:

3 (1) The incurrence by Pinnacle West of over \$750 million in bridge financing
4 (the "Bridge Debt") in direct and justifiable reliance on the 1999 Settlement Agreement,
5 which authorized APS to transfer its generation assets to PWEC (the "asset transfer") by
6 the end of 2002.

7 (2) Given the incurrence of the Bridge Debt, the maintenance of Pinnacle
8 West's credit rating without a downgrade was dependent on PWEC refinancing the bridge
9 debt following the asset transfer.

10 (3) Because it was to be refinanced following the asset transfer at the end of
11 2002, the Bridge Debt is primarily short-dated debt maturing in 2003 and early 2004.

12 (4) PWEC had received a conditional investment-grade BBB credit rating that
13 would have permitted the Bridge Debt to be refinanced by PWEC upon the asset transfer.

14 (5) PWEC has no access to credit in light of Decision No. 65154.

15 Decision No. 65154 now precludes the asset transfer. As APS had warned as far
16 back as last Spring, that Decision has resulted in a severe financial strain on Pinnacle
17 West and in adverse consequences for APS as well, which has already seen a drop in its
18 corporate credit rating since September 10, 2002.

19 At the time Decision No. 65154 was entered, it was anticipated, based on
20 comments during the August 27, 2002 Special Open Meeting, that the Financing
21 Application would be heard in October and decided before the end of 2002. This
22 anticipation of prompt action soon became an assumption by the rating agencies and
23 bankers. However, for various reasons and despite the Company's still outstanding
24 request for an expeditious hearing, the Financing Application has not been scheduled for
25 consideration until next year, with no reasonable expectation of a final order before
26 February 2003.

1 As a result of the regulatory uncertainty surrounding the timing of a Commission
2 decision on the Financing Application and the consequences to Pinnacle West of even a
3 favorable outcome that comes too late to allow for implementation by Spring of 2003, and
4 also due to the significant deterioration in the capital markets since September, Pinnacle
5 West may not be able to renew a \$125 million 364-day bank facility (the "364-day
6 facility"). Indeed, many of Pinnacle West's lenders have advised Pinnacle West that they
7 are simply unwilling to assume the regulatory risk that the Commission will act in a
8 timely and favorable manner, particularly in light of the recent Pinnacle West debt
9 downgrade discussed below. This 364-day facility is necessary to support Pinnacle West's
10 commercial paper program, which program in turn provides the funds used to finance
11 Pinnacle West's ongoing operations. The existing 364-day facility expires on November
12 29, 2002. Without this facility, Pinnacle West will not be able to issue \$125 million of
13 commercial paper, which reduces its continued operational liquidity and has accelerated
14 the problem described in the Financing Application.

15 Also, on November 4, 2002, Standard & Poor's Ratings Services ("S&P") lowered
16 APS' corporate credit rating from BBB+ to BBB, which is the same as the corporate
17 credit rating of Pinnacle West. S&P specifically noted that the ratings downgrade was not
18 a result of the proposal that APS issue \$500 million of debt to refinance Pinnacle West
19 debt. The release stated that "[e]ven on a standalone basis, APS' financial health remains
20 solidly within the triple "B" category even with the addition of \$500 million in debt."
21 Instead, the downgrade reflected S&P's conclusion that APS and its parent should be
22 viewed as a single economic entity from a ratings standpoint. APS' existing debt ratings
23 were not affected at this time. S&P also downgraded Pinnacle West's senior unsecured
24 debt rating from BBB to BBB-. Attachment A is a copy of the S&P press release
25 announcing the ratings downgrade.

26

1 generates, sells and delivers electricity to wholesale customers in the western United
2 States.

3 3. Pinnacle West is the parent company of APS.

4 4. The attorneys for APS in this proceeding, and the individuals upon which all
5 notices and pleadings should be served, are:

6 Thomas L. Mumaw, Esq.
7 Pinnacle West Capital Corporation
8 Law Department
9 P.O. Box 53999
10 Mail Station 8695
11 400 N. 5th Street
12 Phoenix Arizona 85072-3999

13 and

14 Matthew P. Feeney, Esq.
15 Jeffrey B. Guldner, Esq.
16 Snell & Wilmer, LLP
17 One Arizona Center
18 400 E. Van Buren
19 Phoenix, Arizona 85004-0001

20 **THE BACKUP LINE OF CREDIT**

21 5. APS proposes to loan Pinnacle West up to an aggregate principal amount of
22 \$125 million for a period of up to 364 days (the "Backup Line of Credit") or,
23 alternatively, guarantee Pinnacle West debt up to an aggregate principal amount of \$125
24 million for a period of up to 364 days (the "Interim Guarantee"). This should be sufficient
25 to allow Pinnacle West to resolve its immediate liquidity issues and to avoid any further
26 ratings downgrades while the Financing Application is being considered.

6. The terms of the Backup Line of Credit would be substantially similar to the
364-day facility that it replaces. Pinnacle West will pay APS the same or higher
commitment and borrowing fees as under the current 364-day facility. See Attachment B.
The Backup Line of Credit would not result in equivalent economic benefit to Pinnacle

1 West as an actual replacement of the 364-day facility. Instead, from an economic
2 standpoint, the Backup Line of Credit will be the last borrowing choice for Pinnacle West,
3 after the remaining \$125 million commercial paper program and its existing \$300 million
4 bank line of credit, and is designed to be a pure liquidity backstop. The terms of the
5 Interim Guarantee would depend on the terms of the debt guaranteed.

6 7. APS will not be required to borrow any funds to make the Backup Line of
7 Credit or the Interim Guarantee.

8 8. The Backup Line of Credit/Interim Guarantee is only a temporary "fix."
9 Nothing in this Application rescinds, replaces or prejudices the relief requested in the
10 Financing Application or increases the amount of such Application.

11 **CONSEQUENCES IF THE INSTANT APPLICATION IS NOT GRANTED**

12 9. The Backup Line of Credit or Interim Guarantee is necessary to stabilize the
13 financial condition of Pinnacle West and its affiliates and avoid further rating downgrades
14 pending the Commission's decision on the Financing Application.

15 10. Pinnacle West may be unable to renew its 364-day credit facility pending
16 that decision.

17 11. Despite its own financial health, APS has also experienced recent difficulty
18 in syndicating its own bank financing needs as a result of general market conditions, bank
19 sensitivity to the energy market in particular, and, more specifically, concerns about
20 regulatory uncertainty in Arizona. APS believes that any worsening of Pinnacle West's
21 financial position could further impact APS as well, which is already rated by S&P on a
22 unitary basis with Pinnacle West and must have continued free access to national credit
23 markets to fulfill its obligations to its customers.

24 **APS FINANCIAL CONDITION**

25 12. The making of the Backup Line of Credit or Interim Guarantee does not
26

1 anticipate that APS will borrow any funds, does not affect its net income, and would not
2 result in a loss of APS' overall credit quality or debt rating, or in any manner adversely
3 affect APS customers.

4 13. The proposed Backup Line of Credit or Interim Guarantee will not impair
5 the financial status of APS, otherwise prevent it from attracting capital at fair and
6 reasonable terms, or impair the ability of APS to provide safe, reasonable and adequate
7 service.

8 14. Any further deterioration of Pinnacle West's financial condition prior to the
9 Commission's consideration of the Financing Application could adversely impact APS
10 and its customers to the extent it results in an impairment of the Company's ability to
11 access national credit markets on favorable terms.

12 15. In contrast, addressing the current emergency and thus allowing time for
13 eventual consideration of the Financing Application by the Commission will be favorably
14 received by the financial community and will be reflected in their financial assessment of
15 APS.

16 **PRAYER FOR RELIEF**

17 WHEREFORE, the Company asks that the Commission grant at its Open Meeting
18 of November 19, 2002 a partial waiver as to APS of Rule 804(B)(1) and (2) for the
19 purpose of effecting the short-term financing described in this Application. Although no
20 hearing on this Application is required by Rule 806, APS expressly waives any hearing to
21 which it might be otherwise entitled.
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RESPECTFULLY SUBMITTED this 8th day of November 2002.

SNELL & WILMER

By: 
Matthew P. Feeney, Esq.
Jeffrey B. Guldner, Esq.

and

PINNACLE WEST CAPITAL
CORPORATION LAW DEPARTMENT

By: 
Thomas L. Mumaw, Esq.

Attorneys for Arizona Public Service Company

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VERIFICATION

State of Arizona)
) ss.
County of Maricopa)

Barbara M. Gomez, being first duly sworn, states that she is Treasurer of Arizona Public Service Company, the applicant in this matter; that she has read the foregoing application and knows the contents thereof; and that the contents thereof are true and correct to the best of her knowledge and belief.

Barbara M. Gomez

Barbara M. Gomez

Subscribed and sworn to before me
this 5th day of November, 2002.

Christine A. Labrash

Notary Public



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Arizona Public Service Corporate Credit Rating Lowered to 'BBB'

Publication date: 04-Nov-2002

Analyst(s): Kathryn Mock Masterson, San Francisco (1) 415-371-5009

Credit Rating: BBB/Stable/A-2

Rationale

On Nov. 4, 2002, Standard & Poor's Ratings Services affirmed its debt securities ratings of electric utility Arizona Public Service Co. (APS) and lowered the corporate credit rating (CCR) to 'BBB' from 'BBB+'. At the same time, it affirmed the 'BBB' corporate credit rating of Pinnacle West Capital Corp. (PWCC), and lowered its 'BBB' senior unsecured debt rating to 'BBB-'.

The downgrade of the APS CCR is the result of Standard and Poor's conclusion that the regulatory insulation standard is insufficient to warrant a separation of the CCRs between APS and PWCC. The 'BBB' CCR at both entities reflects the consolidated rating of the combined entity.

This action also results in a change in the unsecured debt rating at PWCC because of the structural subordination of this debt as compared to the unsecured debt at APS since the two are viewed as a single economic entity.

The senior secured rating of APS was affirmed at 'A-' due to substantial overcollateralization of the first mortgage bonds and, importantly, management's stated intent not to issue significant

additional secured debt. All first mortgage bonds are callable as of March 2004, which will allow APS to retire its old 1946 master first mortgage bond indenture.

It is important to note that these rating actions are not a result of the company's proposal to move \$500 million of debt from PWCC to APS. Based on Standard & Poor's consolidated rating methodology, the movement of debt from the parent to the subsidiary does not affect the overall financial health of the entities. Even on a stand-alone basis, APS' financial health remains solidly within the 'BBB' category even with the addition of \$500 million in debt.

The ratings reflect the following credit strengths of the consolidated entity:

- Continued ownership of a diverse generation portfolio by APS, which allows the utility to operate as a vertically integrated utility and to recover costs associated with load resource planning. However, the operational risk associated with the retention of generating assets nullifies the anticipated strengthening of APS' business profile;

- The expectation that, although APS will still be required by the ACC, to competitively bid for the portion of its summer peak load that cannot be supplied through current APS assets, the utility will receive regulatory cost recovery for this purchased-power amount; and

- Strong dividends projected from the SunCor subsidiary in the next few years that will be used to reduce the bridge financing debt at PWCC.

The ratings also reflect the following credit concerns:

- About \$550 million in debt matures at PWCC in mid-2003, which places some liquidity pressure on the consolidated entity. Available borrowing capacity under the PWCC bank lines is about \$265 million as of Sept. 30, 2002, although this is expected to decline significantly by July 2003 as the \$300 million bank line is used to finance additional plant expansion at one of PWCC's subsidiaries, Pinnacle West Energy Corp. (PWEC);

- Uncertainty regarding future revenues from PWEC given the ACC's decision to halt the transfer of 4,000 MW in generation assets from APS to PWEC and a requirement that APS bid for the amount of energy not supplied by its own assets. In 2003, PWEC assets will operate as merchant plants and will not have any competitive advantage when competing to serve APS load;

- Increasing amount of consolidated operations coming from unregulated businesses. In 2003, unregulated businesses--principally PWEC and SunCor--are expected to account for 15% of funds from operation; and

- Power cost exposure at APS given the rate freeze that is in place until 2004 and the lack of a power cost adjustment mechanism.

The consolidated financial profile is adequate for current ratings. Cash flow coverage of interest looks strong, however, the capital structure, including the Palo Verde operating lease, is weak when compared with the 'BBB' rating benchmarks. This is projected to improve once capital spending at PWEC decreases (in late 2003) and

capital spending is, once again, concentrated in the regulated rate base of APS needed to satisfy the continued strong growth of the customer base.

Liquidity.

Liquidity is adequate, but will fall to slim levels in mid-2003 when the \$550 million comes due. The company intends to redeem this debt with the \$500 million issue at APS, which will be loaned to PWEC to repay most of the financing. Dividends from APS and SunCor in 2003 and 2004 are expected to be sufficient to repay the remaining amounts. The current ratings reflect the assumption that this repayment will occur and that the \$500 million will be issued at APS.

Outlook

The stable outlook reflects the assumption that the ACC will approve the application by PWCC to issue up to \$500 million at APS to repay a portion of the \$750 million bridge financing at PWCC that was done to build assets at PWEC, as required by the 1999 settlement agreement with the ACC. The addition of two members to the ACC in November 2002 is not expected to have a material change in the support the ACC has recently indicated toward APS' proposal. The issuance at APS should relieve liquidity pressure at PWCC.

Ratings List

Ratings Affirmed

Pinnacle West Capital Corp.

| | |
|-------------------------|----------------|
| Corporate credit rating | BBB/Stable/A-2 |
| Commercial paper | A-2 |

Arizona Public Service Co.

| | |
|---------------------------------------|------------|
| Senior secured debt | A- |
| Senior unsecured debt | BBB |
| Secured lease obligation bonds | BBB |
| Commercial paper | A-2 |

Ratings Lowered

Arizona Public Service Co.

| | To | From |
|-------------------------|----------------|-----------------|
| Corporate credit rating | BBB/Stable/A-2 | BBB+/Stable/A-2 |

Pinnacle West Capital Corp.

| | | |
|-----------------------|------|-----|
| Senior unsecured debt | BBB- | BBB |
|-----------------------|------|-----|

Complete ratings information is available to subscribers of RatingsDirect, Standard & Poor's Web-based credit analysis system, at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www2.standardandpoors.com; under Fixed Income in the left navigation

bar, select Credit Ratings Actions.

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\$125,000,000

364-DAY CREDIT AGREEMENT

dated as of

November __, 2002

between

Pinnacle West Capital Corporation

and

Arizona Public Service Company

AGREEMENT dated as of November __, 2002 between PINNACLE WEST CAPITAL CORPORATION, as Borrower, and ARIZONA PUBLIC SERVICE COMPANY, as Lender.

The parties hereto agree as follows:

ARTICLE 1

Definitions

SECTION 1.01. *Definitions.* The following terms, as used herein, have the following meanings:

“Annual Interest Requirements” means an amount equal to:

- (i) interest on long-term debt for such period as reported in the consolidated income statement for such period, *plus*
- (ii) interest on short-term debt for such period as reported in the consolidated income statement for such period, *plus*
- (iii) imputed interest on the Sale Leaseback Obligation Bonds for such period, such amount being equal to the product of (A) the principal amount of Sale Leaseback Obligation Bonds outstanding during such period and (B) the rate of interest applicable to such Sale Leaseback Obligation Bonds during such period, *plus*
- (iv) all rental payments in respect of operating leases (excluding any portion of such rental payments attributable to operating expenses and excluding any payments in respect of Sale Leaseback Obligation Bonds) with respect to which the payment obligations of the Borrower or a Consolidated Subsidiary of the Borrower have a present value of at least \$25,000,000.

“APS” means the Arizona Public Service Company, an Arizona corporation, and its successors.

“Authorized Officer” means the Chairman of the Board, Chief Executive Officer, President, Treasurer, Controller, Chief Operating Officer, Chief Financial Officer, any Vice President or any Assistant Treasurer of the Borrower.

“Base Rate” means, for any day, a rate per annum equal to the higher of (i) the Prime Rate for such day and (ii) the sum of ½ of 1% plus the Federal Funds Rate for such day.

“Base Rate Loan” means a Loan that bears interest at the Base Rate pursuant to the applicable Notice of Borrowing or Notice of Interest Rate Election or the last sentence of Section 2.08(a).

“Base Rate Margin” has the meaning specified in the Pricing Schedule.

“Benefit Arrangement” means at any time an employee benefit plan within the meaning of Section 3(3) of ERISA which is not a Plan or a Multiemployer Plan and which is maintained or otherwise contributed to by any member of the ERISA Group.

“Borrower” means Pinnacle West Capital Corporation, an Arizona corporation, and its successors.

“Borrower’s 2001 Form 10-K” means the Borrower’s annual report on Form 10-K for the fiscal year ended December 31, 2001, as filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934.

“Borrower’s Latest Form 10-Q” means the Borrower’s quarterly report on Form 10-Q for the quarter ended September 30, 2002, as filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934.

“Borrower’s SEC Reports” means the Borrower’s 2001 Form 10-K; the Borrower’s quarterly reports on Form 10-Q for the quarters ended March 31, 2002, June 30, 2002, and September 30, 2002; and the Borrower’s current reports on Form 8-K dated December 14, 2001, February 8, 2002, March 31, 2002, April 26, 2002, May 22, 2002, June 5, 2002, June 11, 2002, June 30, 2002, July 11, 2002, July 23, 2002, August 13, 2002, August 27, 2002, September 10, 2002, and October 17, 2002.

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

“Commitment” means \$125,000,000; *provided* that, if the context so requires, the term “Commitment” means the obligation of the Lender to extend credit up to such amount to the Borrower hereunder.

“Confidential Information” means information that the Borrower furnishes to the Lender in writing designated as confidential or that the Lender obtains pursuant to its rights under Section 5.01(i) or 5.11, but does not include any such information that (a) is or becomes generally available to the public other than as a result of a breach by the Lender of its obligations hereunder, (b) was available to such party on a nonconfidential basis prior to its disclosure to such party by the Borrower or any of its affiliates or (c) is or becomes available to the Lender from a source other than the Borrower that is not, to the knowledge of such party, acting in violation of a confidentiality agreement with the Borrower.

“Consolidated Capitalization” means the sum of (a) Consolidated Debt and (b) Consolidated Net Worth.

“Consolidated Debt” means at any date the Debt of the Borrower and its Consolidated Subsidiaries determined on a consolidated basis as of such date.

“Consolidated Net Worth” means the sum of (a) the par value (or value stated on the books of the Borrower) of all classes of capital stock of the Borrower and its Subsidiaries, excluding the Borrower’s capital stock owned by the Borrower and/or its Subsidiaries, plus (or minus in the case of a surplus deficit) (b) the amount of the consolidated surplus, whether capital or earned, of the Borrower, determined in accordance with generally accepted accounting principles as of the end of the most recent calendar month (excluding (x) cumulative charges of up to \$300 million to consolidated surplus resulting from, or in anticipation of, discontinuation of FASB 71, accounting for all or part of the business and (y) the effect on the Borrower’s accumulated other comprehensive income/loss of the ongoing application of FASB 133).

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

“Credit Exposure” means (i) the amount of the Lender's Commitment (whether used or unused) at such time or (ii) if the Commitment has terminated in its entirety, the aggregate outstanding principal amount of Lender's Loans at such time.

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

“Default” means any condition or event which constitutes an Event of Default or which with the giving of notice or lapse of time or both would, unless cured or waived, become an Event of Default.

“Derivative Obligations” of any Person means all obligations of such Person in respect of any rate swap transaction, basis swap, forward rate transaction, commodity swap, commodity option, equity or equity index swap, equity or equity index option, bond option, interest rate option, foreign exchange transaction, cap transaction, floor transaction, collar transaction, currency swap transaction, cross-currency rate swap transaction, currency option or any other similar transaction (including any option with respect to any of the foregoing transactions) or any combination of the foregoing transactions.

“Domestic Business Day” means any day except a Saturday, Sunday, or other day on which commercial banks in Phoenix, Arizona are authorized or required by law to close.

“Effective Date” means the date the Commitment becomes effective in accordance with Section 3.01.

“Environmental Laws” means any and all federal, state, local and foreign statutes, laws, judicial decisions, regulations, ordinances, rules, judgments, orders, decrees, plans, injunctions, permits, concessions, grants, franchises, licenses, agreements and other governmental restrictions relating to the environment, the effect of the environment on human health or to emissions, discharges or releases of pollutants, contaminants, Hazardous Substances or wastes into the environment including, without limitation, ambient air, surface water, ground water, or land, or otherwise relating to the manufacture, processing, distribution, use, treatment, storage, disposal, transport or handling of pollutants, contaminants, Hazardous Substances or wastes or the clean-up or other remediation thereof.

“ERISA” means the Employee Retirement Income Security Act of 1974, as amended, or any successor statute.

“ERISA Group” means the Borrower, any Subsidiary and all members of a controlled group of corporations and all trades or businesses (whether or not incorporated) under common control which, together with the Borrower or any Subsidiary are treated as a single employer under Section 414 of the Internal Revenue Code.

“Euro-Dollar Business Day” means any Domestic Business Day on which commercial banks are open for international business (including dealings in dollar deposits) in London.

“Euro-Dollar Loan” means a Loan that bears interest at a Euro-Dollar Rate pursuant to the applicable Notice of Borrowing or Notice of Interest Rate Election.

“Euro-Dollar Margin” has the meaning specified in the Pricing Schedule.

“Euro-Dollar Rate” means a rate of interest determined pursuant to Section 2.07(b) on the basis of a London Interbank Offered Rate.

“Events of Default” has the meaning specified in Section 6.01.

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

“Group of Loans” means, at any time, a Group of Loans consisting of (i) all Committed Loans which are Base Rate Loans at such time or (ii) all Euro-Dollar Loans having the same Interest Period at such time.

“Guarantee” means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Debt of any other Person or in any manner

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

"Hazardous Substances" means (i) any toxic, radioactive, caustic or otherwise hazardous substance, as defined by any applicable Environmental Law; (ii) petroleum, its derivatives, by-products and other hydrocarbons; or (iii) any substance having any constituent elements displaying any of the foregoing characteristics, as defined by any applicable Environmental Law.

"Income Available for Debt Service" means an amount equal to:

- (i) consolidated net income of the Borrower and its Consolidated Subsidiaries for such period, *plus*
- (ii) all material non-recurring items which decreased said net income for such period, *minus*
- (iii) all material non-recurring items which increased said net income for such period, *plus*
- (iv) income taxes deducted in determining said net income for such period, *plus*
- (v) total Annual Interest Requirements of the Borrower and its Consolidated Subsidiaries for such period, *plus*
- (vi) depreciation and amortization, and nuclear fuel amortization for such period, *minus*
- (vii) allowance for equity and borrowed funds used during construction for such period, *minus*
- (viii) deferrals as described in Financial Accounting Standards Board Statement No. 71 for such period, *plus or minus*
- (ix) other significant noncash items for such period as may be specified under Financial Accounting Standards Board Statements or other accounting guidelines.

"Indemnitee" has the meaning specified in Section 9.03(b).

"Interest Coverage Ratio" means, with respect to the Borrower and its Consolidated Subsidiaries, for each twelve-month period ending on the last day of each fiscal quarter (determined as of the last day of such fiscal quarter), the ratio of Income Available for Debt Service to, without duplication of any item, Annual Interest Requirements.

“Interest Period” means, with respect to each Euro-Dollar Loan, the period commencing on the date of borrowing specified in the applicable Notice of Borrowing or on the date specified in an applicable Notice of Interest Rate Election and ending one, two, three or six months thereafter, as the Borrower may elect in such notice; *provided* that:

(a) any Interest Period which would otherwise end on a day which is not a Euro-Dollar Business Day shall be extended to the next succeeding Euro-Dollar Business Day unless such Euro-Dollar Business Day falls in another calendar month, in which case such Interest Period shall end on the next preceding Euro-Dollar Business Day;

(b) any Interest Period which begins on the last Euro-Dollar Business Day in a calendar month (or on a day for which there is no numerically corresponding day in the calendar month at the end of such Interest Period) shall, subject to clause (c) below, end on the last Euro-Dollar Business Day in a calendar month; and

(c) any Interest Period which would otherwise end after the Termination Date shall end on the Termination Date.

“Internal Revenue Code” means the Internal Revenue Code of 1986, as amended, or any successor statute.

“Lender” means Arizona Public Service Company, an Arizona corporation, and its successors.

“Lien” means, with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind, or any other type of preferential arrangement that has the practical effect of creating a security interest, in respect of such asset. For the purposes of this Agreement, the Borrower or any Subsidiary shall be deemed to own subject to a Lien any asset which it has acquired or holds subject to the interest of a vendor or lessor under any conditional sale agreement, capital lease or other title retention agreement relating to such asset.

“Loan” means a loan made by the Lender pursuant to Section 2.01; *provided* that, if any such loan or loans (or portions thereof) are combined or subdivided pursuant to a Notice of Interest Rate Election, the term “Loan” shall refer to the combined principal amount resulting from such combination or to each of the separate principal amounts resulting from such subdivision, as the case may be.

“London Interbank Offered Rate” has the meaning specified in Section 2.07(b).

“Material Debt” means Debt (other than the Loans) of the Borrower and/or one or more of its Subsidiaries in an aggregate principal amount exceeding \$10,000,000.

“Material Derivative Obligations” means Derivative Obligations of the Borrower and/or one or more of its Subsidiaries with an aggregate mark-to-market termination amount exceeding \$10,000,000.

“Material Plan” means at any time a Plan or Plans having aggregate Unfunded Liabilities in excess of \$10,000,000.

“Material Subsidiary” means APS, PWEC and each other Subsidiary of the Borrower (other than SunCor Development Company and any of its Subsidiaries) whose consolidated assets exceed 10% of the consolidated assets of the Borrower and its Consolidated Subsidiaries.

“Moody’s” means Moody’s Investors Service, Inc.

“Multiemployer Plan” means, at any time, an employee pension benefit plan within the meaning of Section 4001(a)(3) of ERISA to which any member of the ERISA Group is then making or accruing an obligation to make contributions or has within the preceding five plan years made contributions, including for these purposes any Person which ceased to be a member of the ERISA Group during such five year period.

“Notes” means promissory notes of the Borrower, substantially in the form of Exhibit A hereto, evidencing the Borrower’s obligation to repay the Loans, and **“Note”** means any one of such promissory notes issued hereunder.

“Notice of Borrowing” means a Notice of Borrowing (as defined in Section 2.02).

“Notice of Interest Rate Election” has the meaning specified in Section 2.08(a).

“Outstanding Committed Amount” means, with respect to the Lender at any time, the aggregate outstanding principal amount of its Loans.

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

“Person” means an individual, a corporation, a limited liability company, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

“Plan” means, at any time, an employee pension benefit plan (other than a Multiemployer Plan) which is covered by Title IV of ERISA or subject to the minimum funding standards under Section 412 of the Internal Revenue Code and either (i) is maintained, or contributed to, by any member of the ERISA Group for employees of any member of the ERISA Group or (ii) has at any time within the preceding five years been maintained, or contributed to, by any Person which was at such time a member of the ERISA Group for employees of any Person which was at such time a member of the ERISA Group.

“Pricing Schedule” means the Pricing Schedule attached hereto.

“Prime Rate” means the rate of interest publicly announced by JPMorgan Chase Bank in New York City from time to time as its Prime Rate.

“PWEC” means Pinnacle West Energy Corporation, an Arizona corporation, and its successors.

“Quarterly Payment Dates” mean each March 31, June 30, September 30, and December 31.

“Reference Bank” means the principal London office (or any successor office) of JPMorgan Chase Bank.

“Regulation U” means Regulation U of the Board of Governors of the Federal Reserve System, as in effect from time to time.

“Revolving Credit Period” means the period from and including the Effective Date to but not including the Termination Date.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw-Hill Companies, Inc.

“Sale Leaseback Obligation Bonds” means PVNGS II Funding Corp.’s (i) 7.39% Secured Lease Obligation Bond, Series 1993, due 2005; (ii) 8.00% Secured Lease Obligation Bonds, Series 1993, due 2015; (iii) any other bonds issued by the Borrower in connection with a sale/leaseback transaction; and (iv) any refinancing or refunding of the obligations specified in subclauses (i) through (iii) above.

“Subsidiary” means, as to any Person, any corporation or other entity of which securities or other ownership interests having ordinary voting power to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by such Person. Unless otherwise specified, **“Subsidiary”** means a Subsidiary of the Borrower.

“Termination Date” means November __, 2003.

“Type” refers to the determination whether a Loan is a Base Rate Loan or a Euro-Dollar Loan.

“Unfunded Liabilities” means, with respect to any Plan at any time, the amount (if any) by which (i) the value of all benefit liabilities under such Plan, determined on a plan termination basis using the assumptions prescribed by the PBGC for purposes of Section 4044 of ERISA, exceeds (ii) the fair market value of all Plan assets allocable to such liabilities under Title IV of ERISA (excluding any accrued but unpaid contributions), all determined as of the then most recent valuation date for such Plan, but only to the extent that such excess represents a potential liability of a member of the ERISA Group to the PBGC or any other Person under Title IV of ERISA.

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

“Utilization” means, at any date, the percentage equivalent of a fraction, (i) the numerator of which is the aggregate outstanding principal amount of the Loans at such date (after giving effect to any borrowing, issuance or payment on such date) and the denominator of which is the amount of the Commitment at such date (after giving effect to any reduction on such date). If for any reason the Lender has any Credit Exposure after termination of the Commitment, Utilization shall be deemed to be 100%.

SECTION 1.02. *Accounting Terms and Determinations.* Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared, in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Borrower's independent public accountants) with the most recent audited consolidated financial statements of the Borrower delivered to the Lender; *provided* that, if the Borrower notifies the Lender that the Borrower wishes to amend any covenant in Article 5 to eliminate the effect of any change in generally accepted accounting principles on the operation of such covenant (or if the Lender notifies the Borrower that the Lender wishes to amend Article 5 for such purpose), then the Borrower's compliance with such covenant shall be applied on the basis of generally accepted accounting principles in effect immediately before the relevant change in generally accepted accounting principles became effective, until either such notice is withdrawn or such covenant is amended in a manner satisfactory to the Borrower and the Lender.

SECTION 1.03. *Types of Borrowings.* The term "**Borrowing**" denotes the Type of Loan to be made to the Borrower pursuant to Article 2 on a single date. Borrowings are classified for purposes of this Agreement by reference to the Type of Loans comprising such Borrowing (*e.g.*, a Euro-Dollar Borrowing is a Borrowing comprised of Euro-Dollar Loans).

ARTICLE 2

The Credits

SECTION 2.01. *Commitment to Lend.* The Lender agrees, on the terms and conditions set forth in this Agreement, to make loans to the Borrower pursuant to this Section from time to time during the Revolving Credit Period; *provided* that, immediately after each such loan is made, the Lender's Outstanding Committed Amount shall not exceed its Commitment and each Borrowing under this Section shall be in an aggregate principal amount of \$5,000,000 or any larger integral multiple of \$1,000,000 (except that any such Borrowing may be in the aggregate amount available within the limitations in the foregoing proviso). Within the foregoing limits, the Borrower may borrow under this Section, prepay Loans to the extent permitted by Section 2.11 and reborrow at any time during the Revolving Credit Period under this Section.

SECTION 2.02. *Notice of Borrowing.* The Borrower shall give the Lender notice (a "**Notice of Borrowing**") not later than 12:00 noon (Phoenix time) on (y) the date of each Base Rate Borrowing and (z) the third Euro-Dollar Business Day before each Euro-Dollar Borrowing, specifying:

- (a) the date of such Borrowing, which shall be a Domestic Business Day in the case of a Base Rate Borrowing or a Euro-Dollar Business Day in the case of a Euro-Dollar Borrowing;
- (b) the aggregate amount of such Borrowing;

(c) whether the Loans comprising such Borrowing are to bear interest initially at the Base Rate or a Euro-Dollar Rate; and

(d) in the case of a Euro-Dollar Borrowing, the duration of the initial Interest Period applicable thereto, subject to the provisions of the definition of Interest Period.

SECTION 2.03. [Intentionally Left Blank]

SECTION 2.04. *Notice to Lenders.* (a) After Lender's receipt of a Notice of Borrowing, such Notice of Borrowing shall not thereafter be revocable by the Borrower.

(b) Not later than 12:00 P.M. (Phoenix time) on the date of each Borrowing, the Lender shall make available to Borrower, in Federal or other funds immediately available in Phoenix, Arizona, the amount of funds specified in the Notice of Borrowing.

SECTION 2.05. *Registry; Notes.* (a) The Lender shall maintain a register (the "**Register**") in which it will record each Loan made by the Lender and each repayment of any Loan. Any such recordation by the Lender in the Register shall be conclusive, absent manifest error. Failure to make any such recordation, or any error in such recordation, shall not affect the Borrower's obligations hereunder in respect of the Loans.

(b) The Lender may, by notice to the Borrower, request (i) that its Loans be evidenced by a single Note payable to the order of such Lender in an amount equal to the aggregate unpaid principal amount of such Loans or (ii) that its Loans of a particular Type be evidenced by a separate Note in an amount equal to the aggregate unpaid principal amount of such Loans. Each such Note shall be in substantially the form of Exhibit A hereto with any appropriate modifications to reflect the fact that it evidences solely Loans of a particular Type. Each reference in this Agreement to the "Note" of such Lender shall be deemed to refer to and include any or all of such Notes, as the context may require.

SECTION 2.06. *Maturity of Loans.* Each Loan shall mature, and the principal amount thereof shall be due and payable (together with interest accrued thereon), on the Termination Date.

SECTION 2.07. *Interest Rates.* (a) Each Base Rate Loan shall bear interest on the outstanding principal amount thereof, for each day from the date such Loan is made until it becomes due, at a rate per annum equal to the sum of the Base Rate plus the Base Rate Margin for such day. Such interest shall be payable quarterly in arrears on each Quarterly Payment Date and on the Termination Date and, with respect to the principal amount of any Base Rate Loan that is prepaid or converted to a Euro-Dollar Loan, on the date of such prepayment or conversion.

(b) Each Euro-Dollar Loan shall bear interest on the outstanding principal amount thereof, for each day during each Interest Period applicable thereto, at a rate per annum equal to the sum of the Euro-Dollar Margin for such day plus the London Interbank Offered Rate applicable to such Interest Period. Such interest shall be payable for each Interest Period on the last day thereof and, if such Interest Period is longer than three months, at intervals of three months after the first day thereof and, with respect to the principal amount of any Euro-Dollar

Loan that is prepaid or converted to a Base Rate Loan, on the date of such prepayment or conversion.

The "**London Interbank Offered Rate**" applicable to any Interest Period means (a) the offered rate for dollar deposits, for a period approximately equal to such Interest Period and, if the amount is so quoted, in an amount approximately equal to the average principal amount of the applicable Loans, quoted on the second Euro-Dollar Business Day prior to the first day of such Interest Period, as such rate appears on the display designated as page "3750" on the Telerate service (or such other page as may replace page "3750" on the Telerate service or such other service as may be nominated by the British Bankers' Association as the information vendor for the purpose of displaying British Bankers' Association Interest Settlement Rates for U.S. Dollar deposits) ("**Telerate Page 3750**") as of 11:00 A.M. (London time) on such date, (b) if, as of 11:00A.M. (London time) on any such date such rate does not appear on the Telerate Page 3750, the arithmetic mean (adjusted, if necessary, to the nearest 1/16th of 1%), of the offered rates for dollar deposits, for a period approximately equal to such Interest Period quoted on the second Euro-Dollar Business Day prior to the first day of such Interest Period, as such rates appear on the display designated as page "LIBO" on the Reuters Monitor Money Rates Service (or such other page as may replace the "LIBO" page on that service for the purpose of displaying London interbank offered rates of major banks) ("**Reuters Screen LIBO Page**") as of 11:00 A.M. (London time) on such date, or (c) if neither of the above rates is available (and in the case of clause (b), if on any such date at least two such rates do not appear on the Reuters Screen LIBO page), the average (adjusted, if necessary, to the next higher 1/16th of 1%) of the respective rates per annum at which deposits in dollars are offered to the Reference Bank in the London interbank market at approximately 11:00 A.M. (London time) two Euro-Dollar Business Days before the first day of such Interest Period in an amount approximately equal to the principal amount of the Euro-Dollar Loan to which such Interest Period is to apply and for a period of time comparable to such Interest Period.

(c) [Intentionally Left Blank]

(d) Any overdue principal of and interest on any Loan shall bear interest, payable on demand, for each day from and including the date payment thereof was due to but excluding the date of actual payment, at a rate per annum equal to the sum of 1% plus the Base Rate plus the Base Rate Margin for such day.

(e) The Lender shall determine each interest rate applicable to the Loans hereunder. The Lender shall promptly notify the Borrower of each rate of interest so determined, and its determination thereof shall be conclusive in the absence of manifest error.

SECTION 2.08. *Method of Electing Interest Rates.* (a) The Loans included in each Borrowing shall bear interest initially at the type of rate specified by the Borrower in the applicable Notice of Borrowing. Thereafter, the Borrower may from time to time elect to change or continue the type of interest rate borne by each Group of Loans (subject to Section 2.08(d)), as follows:

(i) if such Loans are Base Rate Loans, the Borrower may elect to convert such Loans to Euro-Dollar Loans as of any Euro-Dollar Business Day; and

(ii) if such Loans are Euro-Dollar Loans, the Borrower may elect to convert such Loans to Base Rate Loans as of any Domestic Business Day, or may elect to continue such Loans as Euro-Dollar Loans, as of the end of any Interest Period applicable thereto, for an additional Interest Period.

Each such election shall be made by delivering a notice (a “**Notice of Interest Rate Election**”) to the Lender not later than 12:00 Noon (Phoenix, Arizona time) on the third Euro-Dollar Business Day before the conversion or continuation selected in such notice is to be effective. A Notice of Interest Rate Election may, if it so specifies, apply to only a portion of the aggregate principal amount of the relevant Group of Loans; *provided* that (i) such portion is allocated ratably among the Loans comprising such Group and (ii) the portion to which such Notice applies, and the remaining portion to which it does not apply, are each at least \$5,000,000 (unless such portion is comprised of Base Rate Loans). If no such notice is timely received before the end of an Interest Period for any Group of Euro-Dollar Loans, the Borrower shall be deemed to have elected that such Group of Loans be converted to Base Rate Loans at the end of such Interest Period.

(b) Each Notice of Interest Rate Election shall specify:

(i) the Group of Loans (or portion thereof) to which such notice applies;

(ii) the date on which the conversion or continuation selected in such notice is to be effective, which shall comply with the applicable clause of Section 2.08(a);

(iii) if the Loans comprising such Group are to be converted, the new Type of Loans and, if the Loans resulting from such conversion are to be Euro-Dollar Loans, the duration of the next succeeding Interest Period applicable thereto; and

(iv) if such Loans are to be continued as Euro-Dollar Loans for an additional Interest Period, the duration of such additional Interest Period.

Each Interest Period specified in a Notice of Interest Rate Election shall comply with the provisions of the definition of Interest Period.

(c) After Lender's receipt of a Notice of Interest Rate Election from the Borrower pursuant to Section 2.08(a), such notice shall not thereafter be revocable by the Borrower.

(d) The Borrower shall not be entitled to elect to convert any Loans to, or continue any Loans for an additional Interest Period as, Euro-Dollar Loans if (i) the aggregate principal amount of any Group of Euro-Dollar Loans created or continued as a result of such election would be less than \$5,000,000 or (ii) a Default shall have occurred and be continuing when the Borrower delivers notice of such election to the Lender.

(e) If any Loan is converted to a different Type of Loan, the Borrower shall pay, on the date of such conversion, the interest accrued to such date on the principal amount being converted.

SECTION 2.09. *Fees.* (a) The Borrower shall pay to the Lender a facility fee calculated for each day at the Facility Fee Rate for such day (determined in accordance with the Pricing Schedule) on the aggregate amount of the Credit Exposures on such day. Such facility fee shall accrue for each day from and including the Effective Date to but excluding the day on which the Credit Exposures are reduced to zero.

(b) The Borrower shall pay to the Lender for each day on which Utilization exceeds 33.3%, a utilization fee at the rate of 0.125% per annum on the sum of the aggregate outstanding principal amount of the Loans on such day.

(c) Fees accrued for the account of the Lenders under this Section shall be payable quarterly in arrears on each Quarterly Payment Date and on the day on which the Commitment terminates in its entirety (and, if later, on the day on which the Credit Exposures are reduced to zero)

SECTION 2.10. *Termination or Reduction of Commitments.* (a) The Borrower may, upon at least three Domestic Business Days' notice to the Lender, (i) terminate the Commitment at any time, if no Loans are outstanding at such time, or (ii) ratably reduce from time to time by an aggregate amount of \$5,000,000 or any larger multiple of \$1,000,000, the amount of the Commitment in excess of the Outstanding Committed Amount.

(b) Unless previously terminated, the Commitment shall terminate in its entirety on the Termination Date.

SECTION 2.11. *Optional Prepayments.* (a) The Borrower may (i) upon at least one Domestic Business Day's notice to the Lender, prepay any Group of Base Rate Loans or (ii) upon at least three Euro-Dollar Business Days' notice to the Lender, prepay any Group of Euro-Dollar Loans, in each case in whole at any time, or from time to time in part in amounts aggregating \$5,000,000 or any larger integral multiple of \$1,000,000, by paying the principal amount to be prepaid together with interest accrued thereon to the date of prepayment.

(b) After Lender's receipt of a notice of prepayment pursuant to this Section, such notice shall not thereafter be revocable by the Borrower.

SECTION 2.12. *General Provisions as to Payments.* The Borrower shall make each payment of principal of, and interest on, the Loans and interest thereon and of fees hereunder not later than 2:00 P.M. (Phoenix time) on the date when due, in Federal or other funds immediately available in Phoenix, Arizona, to the Lender at its address specified in or pursuant to Section 9.01 and without reduction by reason of any set-off or counterclaim. Whenever any payment of principal of, or interest on, the Base Rate Loans or of fees shall be due on a day which is not a Domestic Business Day, the date for payment thereof shall be extended to the next succeeding Domestic Business Day. Whenever any payment of principal of, or interest on, the Euro-Dollar Loans shall be due on a day which is not a Euro-Dollar Business Day, the date for payment thereof shall be extended to the next succeeding Euro-Dollar Business Day unless such Euro-Dollar Business Day falls in another calendar month, in which case the date for payment thereof shall be the next preceding Euro-Dollar Business Day. If the date for

any payment of principal is extended by operation of law or otherwise, interest thereon shall be payable for such extended time.

SECTION 2.13. *Computation of Interest and Fees.* Interest based on the Prime Rate hereunder shall be computed on the basis of a year of 365 days (or 366 days in a leap year) and paid for the actual number of days elapsed (including the first day but excluding the last day). All other interest and fees shall be computed on the basis of a year of 360 days and paid for the actual number of days elapsed (including the first day but excluding the last day).

ARTICLE 3

Conditions

SECTION 3.01. *Effectiveness.* The Commitment shall become effective only when each of the following conditions has been satisfied:

- (a) the Lender and the Borrower shall have each signed this Agreement
- (b) all necessary corporate approvals have been obtained;
- (c) all necessary regulatory approvals, consents, or waivers shall have been obtained, including any required approvals, consents, or waivers of the Arizona Corporation Commission;
- (d) the Lender shall have received all documents the Lender may reasonably request relating to the existence of the Borrower, the corporate authority for and the validity of this Agreement and the Notes, and any other matters relevant hereto, all in form and substance satisfactory to the Lender.

SECTION 3.02. *Borrowings.* The obligation of the Lender to make a Loan on the occasion of any Borrowing is subject to the satisfaction of the following conditions:

- (a) receipt by the Lender of a Notice of Borrowing as required by Section 2.02;
- (b) the fact that, immediately before and after such Borrowing or issuance, no Default shall exist; and
- (c) the fact that the representations and warranties of the Borrower contained in this Agreement shall be true in all material respects on and as of the date of such Borrowing.

Each Borrowing hereunder shall be deemed to be a representation and warranty by the Borrower on the date of such Borrowing as to the facts specified in the foregoing clauses 3.02(b) and 3.02(c).

ARTICLE 4

Representations and Warranties

The Borrower represents and warrants that:

SECTION 4.01. *Corporate Existence and Power.* The Borrower is a corporation duly incorporated, validly existing and in good standing under the laws of Arizona, and has all corporate powers and all material governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted, unless the failure to have any such license, authorization, consent or approval would not have a material adverse affect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries taken as a whole.

SECTION 4.02. *Corporate and Governmental Authorization; No Contravention.* The execution, delivery and performance by the Borrower of this Agreement and the Notes are within the Borrower's corporate powers, have been duly authorized by all necessary corporate action, require no action by or in respect of, or filing with, any governmental body, agency or official and do not contravene, or constitute a default under, any provision of applicable law or regulation or of the certificate of incorporation or by-laws of the Borrower or of any agreement, judgment, injunction, order, decree or other instrument binding upon the Borrower or any Material Subsidiary or result in the creation or imposition of any Lien on any asset of the Borrower or any Material Subsidiary.

SECTION 4.03. *Binding Effect.* This Agreement constitutes a valid and binding agreement of the Borrower and each Note, when executed and delivered in accordance with this Agreement, will constitute a valid and binding obligation of the Borrower, in each case enforceable in accordance with its terms; subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

SECTION 4.04. *Financial Information.* (a) The consolidated balance sheet of the Borrower and its Consolidated Subsidiaries as of December 31, 2001 and the related consolidated statements of income and of cash flow for the fiscal year then ended, reported on by Deloitte & Touche LLP and set forth in the Borrower's 2001 Form 10-K, fairly present, in conformity with generally accepted accounting principles (except as disclosed therein), the consolidated financial position of the Borrower and its Consolidated Subsidiaries as of such date and their consolidated results of operations and cash flows for such fiscal year.

(b) The unaudited consolidated balance sheet of the Borrower and its Consolidated Subsidiaries as of September 30, 2002 and the related unaudited consolidated statements of income and of cash flows for the nine months then ended, set forth in the Borrower's Latest Form 10-Q, fairly present, in conformity with generally accepted accounting principles applied on a basis consistent with the financial statements referred to in subsection (a) of this Section (except as disclosed therein), the consolidated financial position of the Borrower and its Consolidated Subsidiaries as of such date and their consolidated results of operations and cash flows for such nine month period (subject to normal year-end adjustments).

(c) Except as disclosed in the Borrower's SEC Reports, since December 31, 2001 there has been no material adverse change in the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, considered as a whole.

SECTION 4.05. *Litigation.* Except as disclosed in the Borrower's SEC Reports, there is no action, suit or proceeding pending against, or to the knowledge of the Borrower threatened against or affecting, the Borrower or any of its Subsidiaries before any court or arbitrator or any governmental body, agency or official in which there is a reasonable possibility of an adverse decision which could materially adversely affect the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, considered as a whole, or which in any manner draws into question the validity of this Agreement or the Notes.

SECTION 4.06. *Compliance with ERISA.* Each member of the ERISA Group has fulfilled its obligations under the minimum funding standards of ERISA and the Internal Revenue Code with respect to each Plan and is in compliance in all material respects with the presently applicable provisions of ERISA and the Internal Revenue Code with respect to each Plan. No member of the ERISA Group has (i) sought a waiver of the minimum funding standard under Section 412 of the Internal Revenue Code in respect of any Plan, (ii) failed to make any contribution or payment to any Plan or Multiemployer Plan or in respect of any Benefit Arrangement, or made any amendment to any Plan or Benefit Arrangement, which has resulted or could result in the imposition of a Lien or the posting of a bond or other security under ERISA or the Internal Revenue Code or (iii) incurred any liability under Title IV of ERISA other than a liability to the PBGC for premiums under Section 4007 of ERISA.

SECTION 4.07. *Environmental Matters.* Except as disclosed in the Borrower's SEC Reports, the operations and properties of the Borrower and its Material Subsidiaries comply in all material respects with all Environmental Laws, except where (i) the necessity of compliance therewith is being contested in good faith by appropriate proceedings or (ii) the noncompliance with which would not have a material adverse effect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries taken as a whole.

SECTION 4.08. *Taxes.* The Borrower and its Material Subsidiaries have filed all United States Federal income tax returns and all other material tax returns which are required to be filed by them and have paid all taxes due pursuant to such returns or pursuant to any assessment received by them, except to the extent that such taxes are being contested in good faith and by appropriate proceedings and that appropriate reserves for the payment thereof have been maintained by the Borrower or its Material Subsidiaries in accordance with generally accepted accounting principles. The charges, accruals and reserves on the books of the Borrower in respect of taxes or other governmental charges are, in the opinion of the Borrower, adequate.

SECTION 4.09. *Material Subsidiaries.* Each Material Subsidiary is duly organized, validly existing and in good standing under the laws of its jurisdiction of organization, and, except as disclosed in the Borrower's SEC Reports, has all corporate and other legal powers and all material governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted, except where the failure to have any such license, authorization, consent or approval would not have a material adverse affect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries taken as a whole, and as to APS, except that (i) APS from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (ii) from time to time communities served by APS may become incorporated and considerable time may elapse before such a franchise is procured, (iii) certain

such franchises may have expired prior to the renegotiation thereof, (iv) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (v) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope.

SECTION 4.10. *Not an Investment Company.* The Borrower is not an "investment company" within the meaning of the Investment Company Act of 1940, as amended.

SECTION 4.11. *Public Utility Holding Company Act, Etc.* The Borrower is a "holding company" within the meaning of the Public Utility Holding Company Act of 1935, as amended; however, pursuant to Section 3(a)(1) of such Act and Rule 2 promulgated thereunder, the Borrower is exempt from all provisions of such Act other than Section 9(a)(2) thereof. The Borrower warrants that it is a "public utility", as such term is defined in the Federal Power Act, as amended, which has obtained blanket authority from the Federal Energy Regulatory Commission to issue securities and assume liabilities.

SECTION 4.12. *Full Disclosure.* All information (other than financial projections) heretofore furnished by the Borrower in writing to the Lender for purposes of or in connection with this Agreement or any transaction contemplated hereby is, and all such information (other than financial projections) hereafter furnished by the Borrower to the Lender in connection with this Agreement will be, true and accurate in all material respects on the date as of which such information is furnished. The financial projections that have been or will be furnished by the Borrower to the Lender for purposes of or in connection with this Agreement or any transaction contemplated hereby were or will be prepared in good faith based upon reasonable assumptions. The Borrower has disclosed to the Lender in writing (including through the Borrower's SEC Reports) any and all facts which materially and adversely affect or may materially and adversely affect (to the extent the Borrower can now reasonably foresee), the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, taken as a whole, or the ability of the Borrower to perform its obligations under this Agreement.

ARTICLE 5

Covenants

The Borrower agrees that, so long as the Lender has any Credit Exposure hereunder:

SECTION 5.01. *Information.* The Borrower will deliver to the Lender:

(a) as soon as available and in any event within 120 days after the end of each fiscal year of the Borrower, a consolidated balance sheet of the Borrower and its Consolidated Subsidiaries and an unconsolidated balance sheet of the Borrower as of the end of such fiscal year and the related consolidated and unconsolidated statements of income and a consolidated statement of cash flow for such fiscal year, setting forth in each case in comparative form the figures for the previous fiscal year, accompanied by an opinion thereon of Deloitte & Touche LLP or other independent certified public accountants of recognized public standing, which opinion shall state that said financial statements fairly present in all material respects the financial condition and results of operations of the Borrower and its Consolidated Subsidiaries as

at the end of, and for, such fiscal year, in accordance with generally accepted accounting principles consistently applied (except as disclosed therein);

(b) as soon as available and in any event within 60 days after the end of each of the first three quarters of each fiscal year of the Borrower, a consolidated balance sheet of the Borrower and its Consolidated Subsidiaries and an unconsolidated balance sheet of the Borrower as of the end of such quarter and the related consolidated and unconsolidated statements of income and a consolidated statement of cash flow for such quarter and for the portion of the Borrower's fiscal year ended at the end of such quarter, setting forth in the case of such statements of income and of cash flow in comparative form the figures for the corresponding quarter and the corresponding portion of the Borrower's previous fiscal year, accompanied by a certificate of an Authorized Officer, which certificate shall state that said financial statements fairly present the financial condition and results of operations of the Borrower and its Consolidated Subsidiaries in accordance with generally accepted accounting principles, consistently applied (except as disclosed therein), as at the end of, and for, such period (subject to normal year-end audit adjustments);

(c) simultaneously with the delivery of each set of financial statements referred to in clauses (a) and (b) above, a certificate of an Authorized Officer of the Borrower (i) setting forth in reasonable detail the calculations required to establish whether the Borrower was in compliance with the requirements of Sections 5.06, 5.09 and 5.10 on the date of such financial statements and (ii) stating whether any Default exists on the date of such certificate and, if any Default then exists, setting forth the details thereof and the action which the Borrower is taking or proposes to take with respect thereto;

(d) as soon as possible and in any event within five Domestic Business Days after an Authorized Officer obtains knowledge of any Default, if such Default is then continuing, a certificate of an Authorized Officer setting forth the details thereof and the action which the Borrower is taking or proposes to take with respect thereto;

(e) promptly upon the mailing thereof to the shareholders of the Borrower generally, copies of all financial statements, reports and proxy statements so mailed;

(f) promptly upon the filing thereof, copies of all registration statements (other than the exhibits thereto and any registration statements on Form S-8 or its equivalent) and reports on Forms 10-K, 10-Q and 8-K (or their equivalents) which the Borrower shall have filed with the Securities and Exchange Commission;

(g) if and when any member of the ERISA Group (i) gives or is required to give notice to the PBGC of any "reportable event" (as defined in Section 4043 of ERISA) with respect to any Plan which might constitute grounds for a termination of such Plan under Title IV of ERISA, or knows that the plan administrator of any Plan has given or is required to give notice of any such reportable event, a copy of the notice of such reportable event given or required to be given to the PBGC; (ii) receives notice of complete or partial withdrawal liability under Title IV of ERISA or notice that any Multiemployer Plan is in reorganization, is insolvent or has been terminated, a copy of such notice; (iii) receives notice from the PBGC under Title IV of ERISA of an intent to terminate, impose liability (other than for premiums under Section 4007

of ERISA) in respect of, or appoint a trustee to administer any Plan, a copy of such notice; (iv) applies for a waiver of the minimum funding standard under Section 412 of the Internal Revenue Code, a copy of such application; (v) gives notice of intent to terminate any Plan under Section 4041(c) of ERISA, a copy of such notice and other information filed with the PBGC; (vi) gives notice of withdrawal from any Plan pursuant to Section 4063 of ERISA, a copy of such notice; or (vii) fails to make any payment or contribution to any Plan or Multiemployer Plan or in respect of any Benefit Arrangement or makes any amendment to any Plan or Benefit Arrangement which has resulted or could result in the imposition of a Lien or the posting of a bond or other security under ERISA and the Internal Revenue Code, a certificate of an Authorized Officer setting forth details as to such occurrence and action, if any, which the Borrower or applicable member of the ERISA Group is required or proposes to take; and

(h) promptly after an Authorized Officer becomes aware of the occurrence thereof, notice of any change by Moody's or S&P of their respective ratings referenced in the Pricing Schedule or of the cessation (or subsequent commencement) by Moody's or S&P of publication of their respective ratings referenced in the Pricing Schedule; and

(i) from time to time such additional information regarding the financial position or business of the Borrower and its Subsidiaries as the Lender, may reasonably request.

Information required to be delivered pursuant to Sections 5.01(a), 5.01(b), 5.01(e) or 5.01(f) above shall be deemed to have been delivered on the date on which the Borrower provides notice to the Lender that such information has been posted on the Borrower's website on the Internet at the website address listed on the signature pages hereof, at sec.gov/edaux/searches.htm or at another website identified in such notice and accessible by the Lender without charge; *provided* that (i) such notice may be included in a certificate delivered pursuant to Section 5.01(c) and (ii) the Borrower shall deliver paper copies of the information referred to in Sections 5.01(a), 5.01(b), 5.01(e) or 5.01(f) to the Lender if it requests such delivery.

SECTION 5.02. *Maintenance of Property; Insurance.* (a) The Borrower will keep, and will cause each Material Subsidiary to keep, all property useful and necessary in its business in good working order and condition, ordinary wear and tear excepted, unless the failure to do so would not have a material adverse effect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, considered as a whole, it being understood that this covenant relates only to the working order and condition of such properties and shall not be construed as a covenant not to dispose of properties.

(b) The Borrower will maintain, and cause each Material Subsidiary to maintain, insurance with responsible and reputable insurance companies or associations in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which the Borrower or such Material Subsidiary operates; *provided, however*, that the Borrower and each Material Subsidiary may self-insure to the same extent as other companies engaged in similar businesses and owning similar properties in the same general areas in which the Borrower or such Material Subsidiary operates.

SECTION 5.03. *Conduct of Business and Maintenance of Existence.* (a) The Borrower will preserve and maintain, and will cause each Material Subsidiary to preserve and maintain, its corporate existence and all rights and privileges (other than, in the case of APS, "franchises" as described in Arizona Revised Statutes, Section 40-283 or any successor provision) reasonably necessary in the normal conduct of its business, unless the failure to maintain such rights or privileges would not have a material adverse effect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, considered as a whole, and will cause APS to use its best efforts to preserve and maintain such franchises reasonably necessary in the normal conduct of its business, except that (i) APS from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (ii) from time to time communities served by APS may become incorporated and considerable time may elapse before such a franchise is procured, (iii) certain such franchises may have expired prior to the renegotiation thereof, (iv) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (v) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope.

(b) The Borrower will continue to conduct, directly or through its Subsidiaries, the same general type of business conducted by the Borrower and its Material Subsidiaries on the date hereof.

SECTION 5.04. *Compliance with Laws.* The Borrower will comply, and cause each Material Subsidiary to comply, in all material respects with all applicable laws, ordinances, rules, regulations, and requirements of governmental authorities (including, without limitation, Environmental Laws and ERISA and the rules and regulations thereunder) except where (i) the necessity of compliance therewith is contested in good faith by appropriate proceedings or (ii) the noncompliance with which would not have a material adverse effect on the financial condition or financial prospects of the Borrower and its Consolidated Subsidiaries, considered as a whole.

SECTION 5.05. *Pari Passu.* The Borrower will not create, assume or suffer to exist any Lien on any of the capital stock of any Material Subsidiary owned by the Borrower or on any Debt of a Material Subsidiary owed to the Borrower unless the Lender is also granted a Lien thereon on a pari passu basis securing all of the Borrower's obligations under this Agreement and the Notes.

SECTION 5.06. *Ownership of APS.* The Borrower will at all times continue to own directly at least 80% of the outstanding capital stock of APS and PWEC.

SECTION 5.07. *Consolidations, Mergers and Sales of Assets.* The Borrower will not (i) consolidate or merge with or into any other Person or (ii) sell, lease or otherwise transfer, directly or indirectly, all or substantially all of the assets of the Borrower and its Subsidiaries, taken as a whole, to any other Person, except that the Borrower may consolidate with or merge into any other corporation if (x) the Borrower is the surviving corporation or (y) the Borrower is not the surviving corporation and (A) the surviving corporation is a corporation organized and existing under the laws of the United States of America or a state thereof or the District of Columbia, with a substantial portion of its assets located and a substantial portion of its business

conducted within the United States and (B) such corporation expressly assumes, by an agreement reasonably satisfactory in substance and form to the Lender (which agreement may require the delivery in connection with such assumption of such opinions of counsel as the Lender may reasonably require) the obligations of the Borrower under this Agreement and the Notes, and (z) immediately after giving effect to such transaction and such assumption, no Default shall have occurred and be continuing.

SECTION 5.08. *Use of Proceeds.* The proceeds of the Loans made under this Agreement will be used by the Borrower to refinance existing indebtedness and for general corporate purposes. None of such proceeds will be used, directly or indirectly, for the purpose, whether immediate, incidental, or ultimate, of buying or carrying any "margin stock" within the meaning of Regulation U; provided, however, that the Borrower may use the proceeds of the Loans made under this Agreement for the purpose of repurchasing shares of the Borrower's common stock so long as such repurchases do not subject any of the Lenders to the requirements of Regulation U in respect of this Agreement.

In accordance with applicable Federal Energy Regulatory Commission orders and precedent, each Loan will be for some lawful object within the corporate purposes of the Borrower, compatible with the public interest, and reasonably necessary or appropriate for such purposes.

SECTION 5.09. *Interest Coverage Ratio.* The Borrower will maintain for each twelve-month period ending on the last day of each fiscal quarter (determined as of the last day of such fiscal quarter) an Interest Coverage Ratio of no less than 2:1.

SECTION 5.10. *Indebtedness.* Consolidated Debt will not exceed at any time an amount equal to 65% of Consolidated Capitalization.

SECTION 5.11. *Inspection of Property, Books and Records.* The Borrower will keep, and will cause each Material Subsidiary to keep, proper books of record and account in which full, true and correct entries shall be made of all dealings and transactions in relation to its business and activities; and will permit, and will cause each Material Subsidiary to permit, representatives of the Lender at the Lender's expense to visit and inspect any of their respective properties, to examine and make abstracts from any of their respective books and records and to discuss their respective affairs, finances and accounts with their respective officers, employees and independent public accountants, all at such reasonable times and as often as may reasonably be desired; provided, however, that the Borrower and its Material Subsidiaries reserve the right to restrict access to any of its properties in accordance with reasonably adopted policies relating to safety and security.

ARTICLE 6

Defaults

SECTION 6.01. *Events of Defaults.* If one or more of the following events ("Events of Default") shall have occurred and be continuing:

(a) the Borrower shall fail to pay (i) when due, any principal of any Loan or (ii) within three Domestic Business Days of the date when due, interest on any Loan, or any fees payable hereunder;

(b) the Borrower shall fail to observe or perform any covenant contained in Sections 5.01(d) and 5.05 to 5.10, inclusive;

(c) the Borrower shall fail to observe or perform any covenant or agreement contained in this Agreement (other than those covered by clause (a) or (b) above) for 30 days after notice thereof has been given to the Borrower by the Lender;

(d) any representation, warranty, certification or statement made by the Borrower in this Agreement or in any certificate, financial statement or other document delivered pursuant to this Agreement shall prove to have been incorrect in any material respect when made (or deemed made);

(e) the Borrower or any Material Subsidiary shall fail to pay any principal of or premium or interest on any Material Debt or Material Derivative Obligation, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Material Debt or Material Derivative Obligation; or the Borrower or any Material Subsidiary shall fail to perform or comply with any other term or covenant in any agreement or instrument relating to such Material Debt or Material Derivative Obligation and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure is to accelerate, or to permit the acceleration of, the maturity of such Material Debt or Material Derivative Obligation;

(f) the Borrower or any Material Subsidiary shall commence a voluntary case or other proceeding seeking liquidation, reorganization or other relief with respect to itself or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, or shall consent to any such relief or to the appointment of or taking possession by any such official in an involuntary case or other proceeding commenced against it, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts as they become due, or shall take any corporate action to authorize any of the foregoing;

(g) an involuntary case or other proceeding shall be commenced against the Borrower or any Material Subsidiary seeking liquidation, reorganization or other relief with respect to it or its debts under any bankruptcy, insolvency or other similar law now or hereafter in effect or seeking the appointment of a trustee, receiver, liquidator, custodian or other similar official of it or any substantial part of its property, and such involuntary case or other proceeding shall remain undismissed and unstayed for a period of 60 days; or an order for relief shall be entered against the Borrower or any Material Subsidiary under the federal bankruptcy laws as now or hereafter in effect;

(h) any member of the ERISA Group shall fail to pay when due an amount or amounts aggregating in excess of \$10,000,000 which it shall have become liable to pay under Title IV of ERISA: or notice of intent to terminate a Material Plan shall be filed under Title IV of ERISA by any member of the ERISA Group, any plan administrator or any combination of the foregoing; or the PBGC shall institute proceedings under Title IV of ERISA to terminate, to impose liability (other than for premiums under Section 4007 of ERISA) in respect of, or to cause a trustee to be appointed to administer any Material Plan; or a condition shall exist by reason of which the PBGC would be entitled to obtain a decree adjudicating that any Material Plan must be terminated; or there shall occur a complete or partial withdrawal from, or a default, within the meaning of Section 4219(c)(5) of ERISA, with respect to, one or more Multiemployer Plans which could cause one or more members of the ERISA Group to incur a current payment obligation in excess of \$10,000,000; or

(i) judgments or orders for the payment of money that exceeds any applicable insurance coverage by more than \$10,000,000 in the aggregate shall be rendered against the Borrower or any Material Subsidiary and such judgments or orders shall continue unsatisfied or unstayed for a period of 45 days;

then, and in every such event, (i) the Lender may, by notice to the Borrower, terminate the Commitments and they shall thereupon terminate, and/or (ii) the Lender may, by notice to the Borrower, declare the Loans (together with accrued interest thereon) to be, and the Loans (together with accrued interest thereon) shall thereupon become, immediately due and payable without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the Borrower; *provided* that in the case of any of the Events of Default specified in clause (f) or (g) above with respect to the Borrower, without any notice to the Borrower or any other act by the Lender, the Commitments shall thereupon terminate and the Loans (together with accrued interest thereon) shall become immediately due and payable without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the Borrower.

ARTICLE 7

[Left Intentionally Blank]

ARTICLE 8

[Left Intentionally Blank]

ARTICLE 9

Miscellaneous

SECTION 9.01. *Notices.* All notices, requests and other communications to any party hereunder shall be in writing (including bank wire, telex, facsimile or similar writing) and shall be given to such party: (a) at its address, facsimile number or telex number set forth on the signature pages hereof, (b) at such other address, facsimile number or telex number as such party may hereafter specify for the purpose by notice to the other party. Each such notice, request or other communication shall be effective (i) if given by telex, when transmitted to the telex number

referred to in this Section and the appropriate answerback is received, (ii) if given by facsimile, when transmitted to the facsimile number referred to in this Section and confirmation of receipt is received, (iii) if given by mail, 72 hours after such communication is deposited in the mails with first class postage prepaid, addressed as aforesaid or (iv) if given by any other means, when delivered at the address referred to in this Section.

SECTION 9.02. *No Waivers.* No failure or delay by the Lender in exercising any right, power or privilege hereunder or under any Note shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies herein provided shall be cumulative and not exclusive of any rights or remedies provided by law.

SECTION 9.03. *Expenses; Indemnification.* (a) The Borrower shall pay (i) all reasonable out-of-pocket expenses of the Lender, including reasonable fees and disbursements of special counsel for the Lender, in connection with the preparation of this Agreement, any waiver or consent hereunder or any amendment hereof or any Default or alleged Default hereunder and (ii) if an Event of Default occurs, all reasonable out-of-pocket expenses incurred by the Lender, including (without duplication) the reasonable fees and disbursements of outside counsel and the reasonable allocated cost of inside counsel, in connection with such Event of Default and any collection, bankruptcy, insolvency, reorganization or other enforcement proceedings resulting therefrom.

(b) The Borrower agrees to indemnify the Lender, its respective affiliates and the respective directors, officers, agents and employees of the foregoing (each an "Indemnitee") and hold each Indemnitee harmless from and against any and all liabilities, losses, damages, costs and expenses of any kind, including, without limitation, reasonable fees and disbursements of counsel, which may be incurred by such Indemnitee in connection with any investigative, administrative or judicial proceeding (whether or not such Indemnitee shall be designated a party thereto) brought or threatened relating to or arising out of this Agreement or any actual or proposed use of proceeds of Loans hereunder; *provided* that no Indemnitee shall have the right to be indemnified hereunder for its own gross negligence or willful misconduct as determined by a court of competent jurisdiction.

SECTION 9.04. [Intentionally Left Blank]

SECTION 9.05. *Amendments and Waivers.* Any provision of this Agreement or the Notes may be amended or waived if, but only if, such amendment or waiver is in writing and is signed by the Borrower and the Lender.

SECTION 9.06. *Successors and Assigns.* The provisions of this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns permitted hereby, except that neither the Borrower nor the Lender may assign or otherwise transfer any of its rights or obligations hereunder (except as provided in Section 5.07) without the prior written consent of the other party (and any attempted assignment or transfer by the Borrower or the Lender without such consent shall be null and void).

SECTION 9.07. *Confidentiality.* The Lender shall exercise the same degree of care that it exercises with respect to its own proprietary information of the same type to maintain the confidentiality of any Confidential Information received pursuant to this Agreement except that disclosure of such Confidential Information may be made (i) to the agents, employees, subsidiaries or affiliates of the Lender in connection with its present or prospective business relations with the Borrower arising out of this Agreement, *provided* that the Lender will cause such agents, employees, subsidiaries or affiliates to comply with the provisions of this Section 9.07 with respect to such Confidential Information, (ii) as required by law, regulations, rule, request or order, subpoena, judicial order or similar order and in connection with any litigation, and (iii) as may be required in connection with the examination, audit or similar investigation of the Lender.

SECTION 9.08. *Governing Law; Jurisdiction.* This Agreement and each Note shall be governed by and construed in accordance with the laws of the State of Arizona. The Borrower hereby submits to the nonexclusive jurisdiction of the United States District Court for the District of Arizona and of any Arizona court sitting in Phoenix, Arizona for purposes of all legal proceedings arising out of or relating to this Agreement or the transactions contemplated hereby. The Borrower irrevocably waives, to the fullest extent permitted by law, any objection which it may now or hereafter have to the laying of the venue of any such proceeding brought in such a court and any claim that any such proceeding brought in such a court has been brought in an inconvenient forum.

SECTION 9.09. *Counterparts; Integration.* This Agreement may be signed in any number of counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument. This Agreement constitutes the entire agreement and understanding among the parties hereto and supersedes any and all prior agreements and understandings, oral or written, relating to the subject matter hereof.

SECTION 9.10. *WAIVER OF JURY TRIAL.* EACH PARTY HERETO HEREBY IRREVOCABLY WAIVES ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective authorized officers as of the day and year first above written.

PINNACLE WEST CAPITAL
CORPORATION

By: _____
Name: Barbara M. Gomez
Title: Treasurer
400 North 5th Street
Phoenix, Arizona 85004
Facsimile number: (602) 250-5640
Website: www.pinnaclewest.com

ARIZONA PUBLIC SERVICE COMPANY

By: _____

Name: Don Robinson

Title: Vice President, Finance and Planning

400 North 5th Street

Phoenix, Arizona 85004

Facsimile number: (602) 250-3399

Website: www.aps.com

364-DAY PRICING SCHEDULE

Each of “**Facility Fee Rate**”, “**Euro-Dollar Margin**” and “**Base Rate Margin**” means, for any day, the rate per annum set forth below in the row opposite such term and in the column corresponding to the Status that applies on such day:

364-Day Facility

| | Level I | Level II | Level III | Level IV | Level V |
|--------------------|---------|----------|-----------|----------|---------|
| Facility Fee Rate | 8.0bp | 10.0bp | 12.5bp | 20.0bp | 30.0bp |
| Euro-Dollar Margin | 42.0bp | 52.5bp | 100.0bp | 130.0bp | 170.0bp |
| Base Rate Margin | 0 | 0 | 0 | 12.5bp | 100.0bp |

For the utilization fee, please see Section 2.09(b).

For purposes of this Schedule, the following terms have the following meanings:

“**Level I Status**” exists at any date if, at such date, the higher of the two Ratings meets the following level:

A- or higher by S&P or A3 or higher by Moody’s.

“**Level II Status**” exists at any date if, at such date, (i) Level I Status does not exist and (ii) the higher of the two Ratings meets the following level:

BBB+ or higher by S&P or Baa1 or higher by Moody’s.

“**Level III Status**” exists at any date if, at such date, (i) neither Level I Status nor Level II Status exists and (ii) the higher of the two Ratings meets the following level:

BBB or higher by S&P or Baa2 or higher by Moody’s.

“**Level IV Status**” exists at any date if, at such date, (i) none of Level I Status, Level II Status and Level III Status exists and (ii) the higher of the two Ratings meets the following level:

BBB- or higher by S&P or Baa3 or higher by Moody’s.

“**Level V Status**” exists at any date if, at such date, no other Status exists.

“**Moody’s**” means Moody’s Investors Service, Inc.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw-Hill Companies, Inc.

“Rating Agencies” means Moody’s and S&P.

“Ratings” means the credit ratings assigned to the senior unsecured long-term debt securities of the Borrower without third-party credit enhancement by the Rating Agencies. If there is no rating assigned to debt securities, the corporate credit rating will be used. Any rating assigned to any other debt security of the Borrower shall be disregarded. The rating in effect at any date is that in effect at the close of business on such date. In the case of split ratings from S&P or Moody’s, the rating to be used to determine which Pricing Level applies is the higher of the two (e.g., BBB+/Baa2 results in Level II Status); *provided* that if the split is more than one full rating category, the rating category immediately above the lower of the two rating categories will be used (e.g., BBB+/Baa3 results in Level III Status, as does A-/Baa3).

“Status” refers to the determination of which of Level I Status, Level II Status, Level III Status, Level IV Status or Level V Status exists at any date.

Exhibit A

NOTE

Phoenix, Arizona

For value received, PINNACLE WEST CAPITAL CORPORATION, an Arizona corporation (the "**Borrower**"), promises to pay to the order of ARIZONA PUBLIC SERVICE COMPANY (the "**Lender**"), the unpaid principal amount of each Loan made by the Lender to the Borrower pursuant to the Credit Agreement (defined below) on the maturity date provided for in the Credit Agreement. The Borrower promises to pay interest on the unpaid principal amount of each such Loan on the dates and at the rate or rates provided for in the Credit Agreement. All such payments of principal and interest shall be made in lawful money of the United States in Federal or other immediately available funds at the office of the Lender, as specified in or pursuant to Section 9.01 of the Credit Agreement.

The date, amount and maturity of each Loan made by the Lender and all repayments of the principal thereof shall be recorded by the Lender and, if the Lender so elects in connection with any transfer or enforcement hereof, appropriate notations to evidence the foregoing information with respect to each such Loan then outstanding may be endorsed by the Lender on the schedule attached hereto, or on a continuation of such schedule attached to and made a part hereof; *provided* that the failure of the Lender to make (or any error in making) any such recordation or endorsement shall not affect the Borrower's obligations hereunder or under the Credit Agreement.

This note is one of the Notes referred to in the 364-Day Credit Agreement dated as of November __, 2002 between Pinnacle West Capital Corporation and Arizona Public Service Company (as the same may be amended from time to time, the "**Credit Agreement**"). Terms defined in the Credit Agreement are used herein with the same meanings. Reference is made to the Credit Agreement for provisions for the prepayment hereof and the acceleration of the maturity hereof.

PINNACLE WEST CAPITAL
CORPORATION

By: _____

Name: _____

Title: _____

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