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ORIGINAL

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James S. Pignatelli
Chairman, President &
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December 19, 2003

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Commissioner William A. Mundell
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007-2996

E-01032C-00-0751
G-01032A-02-0598
E-01933A-02-0914
E-01032C-02-0914
G-01032A-02-0914

RE: December 11, 2003 letter regarding PWCC Renegotiation

Dear Commissioner Mundell:

I received your above referenced letter and would like to address your concerns related to the status of the renegotiation of the Pinnacle West Capital Corporation (PWCC) Purchased Power Agreement ("Agreement") as required by Decision #66028 ("Decision").

Over the course of this year (both before and after the Decision) we have discussed numerous contract structure changes with PWCC with the goal of reducing the rate increase impacts to our customers.

We have continued to have productive conversations with PWCC to restructure the Agreement to provide benefits to our customers and have recently focused on a specific structure (as discussed in the October progress report). While this structure meets many our the goals for a new agreement, given current market conditions, the structure does not result in pricing and terms which we believe are in the long-term interests of our customers. As you are well aware, we are currently experiencing unprecedented high and volatile natural gas prices. This recent run up in natural gas prices for this winter have only compounded these pricing and term issues and is the reason there has been no material change in the renegotiation since the October report.

Given the current market prices and PWCC's good faith negotiations we find it pre-mature to utilize FERC's Alternative Dispute Resolution ("ADR") service in this negotiation. However, we are in the process of evaluating the use of ADR with our outside FERC counsel to determine under which circumstances the service would be beneficial and to streamline the timeline if it is needed.

Arizona Corporation Commission

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Commissioner William A. Mundell
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I appreciate your concern with these renegotiation issues and hope that I have addressed your questions. It is not only the requirement of the Order that keeps UniSource actively pursuing both PWCC renegotiation options and other resource solutions, but our continued commitment to our customers to provide long-term reliable and fairly-priced electric service.

Sincerely,

A handwritten signature in black ink that reads "James S. Pignatelli" followed by a stylized flourish or initials.

James S. Pignatelli

cc: Chairman Marc Spitzer
Commissioner Hatch-Miller
Commissioner Gleason
Commissioner Mayes
Docket Control