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Deborah R. Scott, Director
Utilities Division
ARIZONA CORPORATION COMMISSION
1200 W. Washington
Phoenix, Arizona 85007

RE: APS Code of Conduct; ACC Docket Nos. E-01345A-98-0473; E-01345A-97-0773; and RE-00000C-94-0165

Dear Ms. Scott:

Enclosed please find the Code of Conduct polices and procedures referenced in my letter of January 5, 2000. Also, and per your request of January 10, 2000, the citations for the U.S. Supreme Court decisions alluded to in the January 5th letter are as follows:

- (1) Central Hudson Gas & Electric Corporation v. Public Service Commission of New York, 447 U.S. 557, 100 S. Ct. 2343, 65 L. Ed. 2d 341, 34 P.U.R. 4th 178 (1980);
- (2) Consolidated Edison Company v. Public Service Commission of New York, 447 U.S. 530, 100 S. Ct. 2326, 65 L. Ed. 2d 319, 34 P.U.R. 4th 208 (1980); and
- (3) Pacific Gas & Electric Company v. Public Utilities Commission of California, 475 U.S. 1, 106 S. Ct. 903, 89 L. Ed. 2d 1, 72 P.U.R. 4th 634 (1985).

The Arizona decision referenced was:

Mountain States Telephone & Telegraph Company v. Arizona Corporation Commission, 160 Ariz. 350, 773 P. 2d 455 (1989).

Do not hesitate to have your counsel contact me directly if you or other staff members have any questions or comments.

Sincerely yours,

Snell & Wilmer, L.L.P.

Thomas L. Mumaw
Thomas L. Mumaw

TLM/lr

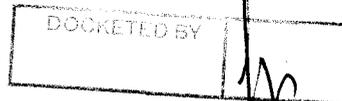
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Deborah R. Scott, Director
Utilities Division
Arizona Corporation Commission
January 12, 2000
Page Two

cc: Carl J. Kunasek, Chairman
Jim Irvin, Commissioner
William A. Mundell, Commissioner
Jerry Rudibaugh
Lyn Farmer, Esq.
All Parties of Record

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CODE OF CONDUCT POLICY	CODE SECTION NO. 4.1.1
SUBJECT: Physical Separation of Entities	

Purpose:

This policy sets forth measures to ensure that APS maintains physical separation from its competitive retail electric affiliates. Physical separation protects against the unauthorized transfer of confidential information and the improper subsidization of its competitive retail electric affiliates.

Policy:

1. Unescorted access to APS-occupied areas is restricted to APS employees, shared services employees and authorized vendors and contractors. Only escorted access to APS-occupied areas will be allowed for employees and agents of a competitive retail electric affiliate and only on an as-needed basis and will under no circumstances allow employees or agents of a competitive retail electric affiliate to read, review, copy or otherwise have access to information that may not be shared with such employees or agents under the Code of Conduct.
2. To control personnel access to APS offices and facilities at Two Arizona Center, the 502 building, the Deer Valley complex, and the Paradise Valley complex, APS shall utilize card-key access security systems. Employee access to these facilities will be granted through security-coded photo identification badges. Each business entity's badges shall be color-coded for clear identification of different business entities. The access security system shall be capable of recording employee access to secured areas.
3. All employees, contractors, visitors and vendors shall be required to wear identification badges in full view when on secured property. Persons without identification badges will be required to obtain a temporary Daily Visitor badge.
4. Pinnacle West Capital Corporation (Pinnacle West) Security shall maintain control over the coding of access available to employees. Pinnacle West Security or any business group or Affiliate may request that Pinnacle West Business Practices make determinations on the status of employee access, as necessary.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NOS. 4.1.2; 4.1.5.1
SUBJECT: Shared Officers and Directors	

Purpose:

The purpose of this policy is to establish appropriate measures to ensure that APS satisfies Section 4.1.5.1 of the Code of Conduct. That provision allows officers and directors of APS to also serve as officers and directors of a competitive retail electric affiliate for purposes of common oversight and governance where sufficient mechanisms are in place so that such sharing does not result in circumventing any of the Code of Conduct provisions.

Policy:

1. An officer or director of APS may serve as an officer or director of a competitive retail electric affiliate for purposes of common oversight and governance under the conditions of this policy.
2. **Officers.** Subject to the conditions below, the Chief Executive Officer of APS may also serve in that capacity with any competitive retail electric affiliate. Additionally, APS may share Support Officers, but shall not share Line Officers, with a competitive retail electric affiliate. Support Officers are officers responsible for corporate support services, including, for example, General Counsel, Secretary, Treasurer, Chief Financial Officer, and Controller. Line Officers are officers directly responsible for operational matters, including, for example, President, Energy Delivery and Sales; President, Generation; Executive Vice President, Generation; Senior Vice President, Nuclear; Vice President, Distribution; Vice President, Nuclear Production; and Vice President, Nuclear Engineering and Support.
3. **Directors.** Subject to the conditions below, a director of APS may also serve as a director of any competitive retail electric affiliate, provided that the director is not also an officer that is not permitted to be shared under this policy.
4. The sharing of the officer or director shall not result in cross-subsidization, nor shall the sharing of the officer or director result in unfair preferential treatment or unfair competitive advantage over other ESPs, in a manner prohibited by the Code of Conduct. The shared support provided by the officer or director shall be priced, reported, and conducted in accordance with APS' Code of Conduct and the policies and procedures implementing the Code of Conduct, including APS' Affiliate Accounting Policies.

5. The shared officer or director shall not allow or facilitate the transfer of information from APS to a competitive retail electric affiliate if the transfer of such information is prohibited by the Code of Conduct and its implementing policies and procedures.
6. The shared officer or director shall review the Code of Conduct, and its implementing policies and procedures upon hiring or promotion and at least annually thereafter. At least annually, the shared officer or director shall also sign a statement of affirmation which states:
 - a. that the officer or director has read and understands the Code of Conduct and its implementing policies and procedures;
 - b. that the officer or director understands the ramifications for violating the Code of Conduct and its implementing policies and procedures; and
 - c. that the sharing of the officer or director satisfies the provisions of the Code of Conduct and its implementing policies and procedures.
7. Pinnacle West Capital Corporation's Business Practices Department shall retain at its offices signed statements of affirmation for a period of five years.
8. APS officers and directors shall retain separate files for any competitive retail electric affiliate for which they are also an officer or director pursuant to this policy. Information obtained from APS and known or retained by such shared officer or director, that cannot be shared with a competitive retail electric affiliate under the Code of Conduct, shall not be conveyed to any other officer, director, or to any employee of a competitive retail electric affiliate, and must remain under the exclusive control of the common officer or director.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 4.1.6
SUBJECT: Contracting for Personnel Services Between APS and Its Competitive Retail Electric Affiliates	

Purpose:

The purpose of this policy is to establish general terms and conditions under which APS and its competitive retail electric affiliates may obtain each other's services.

Policy:

1. The department or employee from whom the services are being contracted must have a recognized expertise needed for the project.
2. The project or assignment must have a specified scope and finite duration (no open-ended contracts, as-needed or on-retainer provisions or "blanket POs").
3. Any competitive retail electric affiliate personnel involved in supporting an APS project or APS personnel involved in supporting a competitive retail electric affiliate project must sign a confidentiality/non-disclosure agreement.
4. All agreements for services between APS and a competitive retail electric affiliate, except for allowable shared services, must be in writing and authorized by both an appropriate officer of APS and an appropriate officer of the competitive retail electric affiliate.
5. All agreements for services must be priced in accordance with APS' Affiliate Accounting Policies.
6. The executed service agreement shall be forwarded to Pinnacle West Capital Corporation Business Practices Department.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 4.1.7
SUBJECT: ESP Contacts and Requests for Service	

Purpose:

The purpose of this policy is to:

- Provide all Electric Service Providers (ESPs), including APS Energy Services, with a single point of contact at APS for initiating requests for Utility Distribution Company (UDC)-provided services and for processing direct access-related requests for service.
- Ensure that APS provides consistent and equitable treatment to all ESPs when handling ESP transactions and requests for UDC-provided services.
- Ensure that APS' actions regarding ESP requests comply with the requirements of the ACC Electric Competition Rules.

Policy:

1. ESP Services is APS' single point of contact for all ESP requests pertaining to direct access processing as well as requests for UDC-provided services.
2. Requests from all ESPs shall be initiated through ESP Services only. Other APS departments and employees shall promptly refer any requests for services received from an ESP to ESP Services for handling and processing or shall advise the ESP to make its request to ESP Services. These departments and employees shall not begin action on an ESP's request for service until notified by ESP Services.
3. ESP Services shall review ESP requests, assign the appropriate organizations to address the requests, determine the appropriate charges, and bill the ESP for the services provided.
4. Requests for UDC-provided services from an APS competitive retail electric affiliate and non-affiliated ESPs shall be processed on a non-discriminatory basis.
5. ESP Services may release information relating to an ESP's request for UDC-provided services only to those APS departments or employees involved in responding to or providing the requested service. Such information will not be released or made available to Affiliates or other APS departments, employees or third parties.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 4.3
SUBJECT: Joint Promotion, Sales and Advertising with a Competitive Retail Electric Affiliate	

Purpose:

The purpose of this policy is to address issues regarding joint promotions, sales and advertising.

Policy:

1. APS will not engage in joint advertising, marketing or sales with a competitive retail electric affiliate.
2. APS will not jointly sponsor civic, industry, or charity functions and events with a competitive retail electric affiliate. For those events sponsored by APS, only the APS name and logo will be used.
3. A competitive retail electric affiliate and APS may participate in the same types of events described above when the event is sponsored by a non-affiliated party; however, they must maintain physically separate booths, displays and/or other facilities. Each facility must bear the name and/or logo of only the company occupying or sponsoring that space or location and may only promote or advertise the services of that company.
4. APS will not provide a competitive retail electric affiliate with preferential treatment over non-affiliated electric service providers (ESPs) regarding the inclusion of advertising materials in customer billings and related customer mailings. APS will also inform non-affiliated ESPs of opportunities to include their advertising materials in APS customer billings or related mailings at the same time and in the same manner that it informs its competitive retail electric affiliate.
5. APS employees will not provide customers with unsolicited information regarding its competitive retail electric affiliate. APS employees can, upon request, provide a customer with the ACC's list of authorized ESPs or provide the ACC's website address for authorized ESPs. If a customer asks an APS employee for information regarding a specific ESP, including APS' competitive retail electric affiliate, the APS employee may provide the customer with a contact name and phone number for the ESP.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 5
SUBJECT: Access to Information	

Purpose:

The purpose of this policy is to address the provision of various types of information by APS to Affiliates.

Policy:

1. Customer-Specific Information

Except as permitted by this Policy, APS shall not provide non-public customer-specific information to any other party, including APSES, unless APS has received written authorization from the customer to provide the information to the other party. Customer-specific information subject to this restriction includes, but is not limited to: name and address; credit and payment history; deposit information; load profile and usage data; and billing information. APS may, however, release customer-specific information without such authorization if required by law (such as in response to a subpoena) or if necessary to obtain collection and payment of a delinquent account or if otherwise authorized by statute or an order or regulation of the ACC.

2. Non-customer Specific Information

Utility Distribution Company (UDC)-Specific Information

APS may provide UDC-specific information (information derived by virtue of APS' status as a UDC and transmission operator), to a competitive retail electric affiliate only if such information is concurrently available to all other ESP's under the same terms and conditions *and* the competitive retail electric affiliate pays the same amount for the information as APS charges other ESPs. UDC-specific information includes, but is not limited to: system resource plans; load growth data; system outage information; extension requests; and transmission access information.

Corporate Administrative Information

APS may provide to Pinnacle West Capital Corporation corporate administrative information that is proprietary and confidential. Corporate administrative information includes, but is not limited to: company policies; personnel policies; shared system information; budgets;

financial reports; company newsletters and employee-related communications; organization charts and benefits information; and material logistics information systems.

Such information provided by APS to Pinnacle West shall not thereafter be provided to a competitive retail electric affiliate unless such sharing is for the purpose of administering shared services, joint corporate oversight, governance, support systems or personnel and the information so provided does not include customer-specific information or UDC-specific information that is not made available to other ESPs in accordance with this procedure.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 7.2
SUBJECT: Training Policy	

Purpose:

The purpose of this policy is to establish appropriate training mechanisms to ensure that APS and its employees comply with the Arizona Corporation Commission (ACC) Electric Competition Rules (the Rules) and the APS Code of Conduct.

Policy:

Program Description:

The APS Code of Conduct Training course content includes:

1. Review of the Rules, paying particular attention to the provisions set forth in the Code of Conduct section of the Rules.
2. Identify and discuss the sections of the APS Code of Conduct that correspond with specific provisions of the Code of Conduct section of the Rules.
3. Use of participatory exercises that reflect some of the typical workplace scenarios that employees may encounter. Employees must identify the Code of Conduct-related issues within the scenarios and develop responses that are appropriate and that comply with the provisions of the Rules and Code of Conduct.

The classes are customized for the various functions throughout APS. For example, the scenarios used for employees working in construction-related functions differ significantly from those used in training employees who work in the Customer Call Center.

The importance of compliance with both the APS Code of Conduct and the Rules is emphasized and, using current industry examples, the consequences of non-compliance are discussed.

The necessity for and expectation of ongoing compliance will also be reflected in Pinnacle West Capital Corporation's (Pinnacle West) Business Practices program.

A companion training program has been developed for and is conducted with the competitive retail electric affiliate's employees.

Participants:

All Utility Distribution Company (UDC) employees need to know the provisions and requirements contained in the Rules and the APS Code of Conduct and understand how those provisions and requirements impact the way they do their jobs.

Those APS employees, whether UDC or not, who have significant customer, ESP, and/or public contact are required to attend the in-depth training sessions. Such employees include, but are not limited to, Distribution Service Leaders, Business Office staff, Call Center staff, Design Project Leaders, Troublemakers and Meter Shop staff and contract personnel in those positions.

Leaders and front-line employees in shared service functions such as Community Relations, Accounting, Finance, and Human Resources, also must attend the in-depth training.

Attendance:

Attendance is mandatory for the UDC employee groups specified above. Attendance is taken at each class for UDC groups and is reported to the UDC's training organization for recording the in Company's database to ensure full participation by UDC Leaders.

New Hire Training Schedule/Reporting:

For newly hired employees, the employee's Leader shall either arrange for or conduct the requisite training. UDC Leaders must also notify Customer Service Training and Development once the employee has completed training in order for the employee's participation to be recorded in APS' database.

Program/Requirement Changes and Revisions:

The course content and materials will be updated as developments and changes occur and subsequent training sessions will be conducted as needed.

For general revisions and updates, Leaders will be provided a copy of the revisions and talking points to share with their teams at the earliest opportunity.

UDC Leaders must notify their training organization to update employee records documenting that employees have been informed of the changes and/or program updates.

Pinnacle West's Business Practices Department will keep a master file of all changes and updates complete with the dates the materials were distributed to Leaders.

Compliance:

Pinnacle West's Business Practices Department will conduct reviews of the UDC's training attendance records in conjunction with periodic self-assessments to ensure UDC compliance in conducting training for new hires and subsequent updates for continuing employees.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NO. 9
SUBJECT: Complaint Resolution	

Purpose:

The purpose of this policy is to document the procedures used by the Pinnacle West Capital Corporation (Pinnacle West) Business Practices Department on behalf of APS to handle complaints concerning violations of the APS Code of Conduct received from APS and its competitive retail electric affiliates' employees and agents.

Background:

The Pinnacle West Business Practices HelpLine (HelpLine), formerly the APS Employee Concerns Line, (1-800-446-8441) was previously established to handle employee concerns. A similar program, known as the Palo Verde Employee Concerns Program exists at the Palo Verde Nuclear site. The HelpLine did not replace the Palo Verde line; but instead it serves the balance of the Pinnacle West family of companies.

The HelpLine is equipped with voice mail so that the program is active 24 hours a day, seven days a week. Voice mail will receive the call during normal working hours if the line is unattended or busy when the call is received. A message is provided to encourage callers to provide sufficient detail when leaving a message.

Scope:

Concerns involving harassment or discrimination in the workplace, unethical behavior, theft, fraud, bribes and/or kickbacks, misuse or abuse of company equipment and materials, alcohol or illegal drug abuse, environmental concerns or safety violations may be raised through the HelpLine. In addition, employees and/or agents of APS may call to receive guidance in the areas of corporate ethics, corporate standards of conduct, regulatory codes/standards of conduct or to report violations of corporate or regulatory codes/standards of conduct.

Responsibility:

The HelpLine is administered by Pinnacle West's Business Practices Department, which reports to the Vice President and General Counsel of Pinnacle West. Confidentiality is a top priority. The program will respect a person's wish to remain anonymous. Although a HelpLine representative

cannot guarantee confidentiality to everyone, whenever possible, the identities of callers will be kept confidential.

If an employee volunteers his/her identity and some disclosure is necessary, reprisal is prohibited. Pinnacle West and its affiliates will not tolerate harassment, intimidation, discrimination, or other acts of retaliation against any employee for identifying any concern, not only to the HelpLine program but also to supervision or management or any governmental agency. Employees who believe they have been discriminated against for identifying a concern should notify Pinnacle West's Human Resources Department or Business Practices Department. If it is determined that an employee or member of management has retaliated against any employee for raising a concern, that person will be subject to appropriate disciplinary action.

Procedures:

Receipt of allegations:

1. Allegations may be received in several ways:
 - Pinnacle West Business Practices HelpLine (1-800-446-8144)
 - Pinnacle West Business Practices HelpLine's internal phone extensions (602-250-3235/2979)
 - Office visit to Pinnacle West Business Practices Department
 - Internal and external mail
 - Referral

2. Each allegation received by the HelpLine will be assigned a unique number when it is received. The number will be provided to the caller as one way of identifying that caller at a later time. In addition to the allegation's number, a unique identifier will be assigned each concern and provided to the caller. The identifier gives one more way of identifying the caller at a later date.

3. The allegation file will include:
 - File Number
 - Identifier
 - Date
 - Time
 - Name
 - Address
 - Type of allegation (confidential or anonymous)
 - Allegation
 - Disposition of the allegation
 - Correspondence related to the allegation

4. Each file related to the APS Code of Conduct will be kept separate from Pinnacle West Business Practices HelpLine files pertaining to non-Code of Conduct-related concerns.
5. Callers will be asked whether or not they request confidentiality. Names of employees requesting confidentiality will not be disclosed to anyone outside the HelpLine program, including investigative assignees, unless there is a "need to know."

Once confidentiality has been requested, the submitter's name may normally be released only with the explicit concurrence of the submitter. If the submitter will not release confidentiality, and release is necessary to address particular concerns, the submitter will be notified that release will be made without their concurrence and the reason why the release is necessary. This decision and action will be thoroughly documented in the respective file.

When confidentiality has been released, the submitter's identity should not be referred to or released to any individual except those determined to have a "need to know." Discretion in the release of confidentiality will be exercised in all cases.

6. Callers not wishing to identify themselves should be told to call back if they wish to receive a report on the status of the concern they have raised. The unique number and identifier will be required before any information will be provided to the caller.

Audit:

This policy will be subject to periodic audits performed by the internal auditors of Pinnacle West.



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CODE OF CONDUCT POLICY	CODE SECTION NOS. 3 and 6
SUBJECT: Affiliate Accounting Policies	

Purpose:

The purpose of these policies is to provide guidelines and standards to ensure compliance with regulatory requirements related to Affiliate relationships. All transactions between APS and its Affiliates, including the provision of services and transfer of assets and liabilities, shall be accounted for in accordance with these policies.

Policies:

I. APPLICABILITY

These Affiliate Accounting Policies set forth business practices for transactions between APS and all Affiliates.

II. COMPLIANCE

The Pinnacle West Capital Corporation (Pinnacle West) Controller is responsible for issuing, updating, and monitoring compliance with these policies and approving specific Affiliate agreements as described below.

III. DEFINITIONS

Affiliate is a separate legal entity that is controlled by, controls, or is under common control with APS.

Assets include real property, depreciable personal property, and intangible property.

Depreciable Personal Property includes vehicles, machinery, furniture, fixtures not attached to land, equipment, computer hardware and related software applications, and any other tangible property, which are not goods or real property.

Fully Loaded Cost consists of the direct cost of a good or service and all applicable indirect charges and overheads.

Goods are non-depreciable personal property, such as inventory, materials and supplies.

Intangible Property includes any asset having no physical existence, its value being set by the rights and anticipated benefits that an owner obtains by possessing it.

Labor Charges consist of direct payroll costs and all wage related costs such as pension, post employment benefits, health insurance, payroll taxes, etc.

Liabilities include accounts payable, notes payable, lease obligations, debt, pension and other post retirement benefits, deferred compensation, and other employee related benefits.

Pinnacle West Capital Corporation (Pinnacle West) is the parent holding company for APS and other Affiliates.

Proprietary Information includes written, verbal, or visual information, material, data, or knowledge belonging to APS or an Affiliate which APS or the Affiliate considers being valuable, confidential, and proprietary. Such proprietary information could be owned by an Affiliate and/or by third parties and licensed to an Affiliate. Proprietary information includes trade secrets, data, software, computer programs and related documentation, specifications, documents, methods, inventions, discoveries, drawings, customer lists, and employee or personnel information and records. Proprietary information also includes information and records relating to research, developments, operations or activities of APS, Affiliates, contractors, or others, which have not been generally released to the public by duly authorized representatives of the entity in lawful possession of the same.

IV. OVERVIEW

These accounting policies provide guidelines and standards to ensure compliance with regulatory accounting requirements related to Affiliate financial relationships, including those requirements of the Arizona Corporation Commission (“ACC”), the Federal Energy Regulatory Commission (“FERC”) and the Securities and Exchange Commission (“SEC”). All transactions between APS and its Affiliates, including the provision of services and transfer of assets or liabilities, shall be accounted for in accordance with these policies.

It is the policy of APS and Pinnacle West to ensure that the costs related to Affiliates are segregated and accounted for separately. Specifically:

- All relationships between APS and its Affiliates are to be conducted in a manner that prevent subsidization of competitive retail electric services provided by such Affiliate through any rate or charge by APS for non-competitive electric services.
- Compensation or reimbursement for all assets, liabilities, goods and services transferred or provided between APS and its Affiliates shall be in accordance with these Affiliate Accounting Policies.
- All transactions between APS and an Affiliate shall be segregated and shall separately account for all costs incurred and revenues received by APS as a result of such transaction.

V. SHARED SERVICES GENERAL

Shared services are those corporate support services performed by Pinnacle West on behalf of its Affiliates. These services are organized at Pinnacle West in order to ensure consistency, efficiency and leverage of resources for the mutual benefit of all Pinnacle West Affiliates. Examples of shared services include the following:

- Accounting and Finance
- Audit
- Tax Services
- Information and Communications Technology
- Corporate Communications
- Shareholder Services
- Law and Business Practices
- Environmental Services
- Public Affairs
- Human Resources

Charges for shared services to the various Affiliates are either direct or indirect. Direct charges result from shared services that benefit a single Affiliate and will be directly assigned to that Affiliate in accordance with this policy. Indirect charges are allocated to the appropriate Affiliate based on a measure representing the Affiliate's proportionate relationship to other Affiliates. The allocation method used is Pinnacle West's net equity invested in its Affiliates. These factors will be reviewed periodically by Pinnacle West Accounting.

A. DIRECT CHARGES

1. Identification

Direct charges are applicable to those shared services that are assignable to a specific Affiliate based on a causal or beneficial relationship to that Affiliate. Where direct shared services benefit more than one Affiliate, such services may be assigned to more than one Affiliate based on the support provided. In other cases, such services will be based on the actual demands for such services by the Affiliate. Examples of direct support services may include some human resources services, information technology support, communications services, and legal services. The provision of direct services will be formalized in a general services agreement.

2. Charging Methodology:

Direct charges are charged to specific Affiliates based on a causal or beneficial relationship or, in the case of special services requested by the Affiliate, on the basis of the service level provided. Direct labor charges will be captured on an "as provided basis" and charged to a specific account number for that Affiliate using variable payroll distribution when the provider can specifically identify the actual hours to provide the service. When the service is provided on a regular or monthly basis and the specific Affiliate is not easily identifiable, as in the case of accounts payable or payroll processing, the time to be charged will be based on a time study or another measurable quantity (i.e., number of invoices processed or number of employees being paid) to

determine the "average" time spent as a percent of total time, with the subsequent use of a payroll fixed distribution.

B. INDIRECT CHARGES

1. Identification:

Indirect charges are those shared services that are essential for the overall corporate enterprise and generally benefit all Affiliates. The associated costs are assignable to each Affiliate. Examples of indirect shared services include preparing consolidated financial statements, filing tax returns, meetings of the Pinnacle West Board of Directors and shareholder services.

2. Charging Methodology:

Because indirect shared services represent functions not specifically identifiable to an Affiliate, it is impractical to charge those costs to the specific Affiliate as the costs are incurred. Therefore, individual employees charge time to Pinnacle West charge numbers when performing those general corporate functions. Indirect charges are allocated to the appropriate Affiliate based on Pinnacle West's net equity invested in its affiliates, including APS.

VI. SERVICES AND GOODS PROVIDED BETWEEN APS AND AFFILIATES

A. GENERAL

This section provides guidelines for the transfer of goods and services, other than shared services described in Section V, between APS and its Affiliates. It provides guidelines to assign monetary value to other goods and services transferred between APS and all Affiliates. There are two general types of transactions that can occur (each of which is discussed in detail at B and C below):

- Goods or services produced, purchased or developed for sale
- Goods or services not produced, purchased, or developed for sale

B. GOODS OR SERVICES PRODUCED, PURCHASED OR DEVELOPED FOR SALE

1. Identification:

Goods or services produced, purchased, or developed for sale include those goods or services intended for sale in the normal course of APS' or the Affiliate's business. To be considered produced, purchased, or developed for sale, the goods and services must be routinely available to third parties in addition to Affiliates and APS and would usually be the product of resources which are planned and dedicated to providing those goods or services. The provision of such goods and services between APS and Affiliates should be formalized in writing and approved by the appropriate Affiliate Officer and Pinnacle West's Controller (or designee), except for goods and services provided pursuant to authorized ACC or FERC tariffs.

Goods or services produced, purchased, or developed for sale include, but are not limited to:

- Electric generation, transmission, and distribution services
- Engineering and development services

2. Charging Methodology:

Goods and services produced, purchased, or developed for sale will be priced based on the following:

From APS to Affiliates:

- Tariff price for services subject to a tariff.
- Market price for services not subject to tariff price and for which a market price for comparable services is readily identifiable (i.e., the good or service is regularly traded on a recognizable market; APS has received a recent, bona fide offer for a comparable good or service; APS has purchased the good or service within the last 6 months from an outside source).
- At fully loaded cost of providing the good or service where there is no readily identifiable market price.

From Affiliates to APS:

- At a price not to exceed market price where a readily determinable market price for comparable services exists (i.e., the good or service is regularly traded on a recognizable market; APS has received a recent, bona fide offer; APS has purchased the good or service within the last 6 months from an outside source).
- At a price not to exceed fully loaded costs where a readily determinable market price does not exist.

3. Recording:

Goods or services produced, purchased or developed for sale will be a direct charge to the recipient Affiliate or APS based upon the pricing described above.

C. GOODS OR SERVICES NOT PRODUCED, PURCHASED, OR DEVELOPED FOR SALE

1. Identification: Goods or services not produced, purchased, or developed for sale include those goods or services that are provided only incidentally to the primary business of APS or an Affiliate and are not provided to unaffiliated third parties. These services (excluding corporate shared services) include but are not limited to:

- Directly requested Affiliate services
- Market analysis
- Research and development

An Affiliate's use of APS' resources or APS' use of an Affiliate's resources shall be supported by a general service agreement.

a. Labor:

No APS employee may perform any work for an Affiliate unless a written agreement is in place. Service agreements must price all goods and services provided in accordance with the provisions for Goods and Services Produced, Purchased or Developed for sale. All costs incurred by APS and revenues received on account of such service agreements shall be recorded in accordance with section VI-B-3 above. Where a service agreement calls for direct labor charges, such labor charges will be based on the rate for that employee and the actual number of hours devoted to providing services. All direct labor will be priced at fully loaded cost by Pinnacle West Accounting, with overhead rates that are updated annually. These overhead rates include associated employee benefits, payroll taxes, performance incentive plan, workers compensation, and other administrative and general costs.

b. Materials:

Purchases of materials or services by an Affiliate from APS or by APS from an Affiliaterequire the preparation of a requisition form. The materials requisition or purchase order should charge the cost to the appropriate Affiliate charge numbers.

2. Charging Methodology:

Goods and services not produced, purchased, or developed for sale will be priced based on the following:

From APS to Affiliates:

- At the market price for services and for which a market price for comparable services is readily identifiable (as defined in section VI-B-2 above).
- At the fully loaded cost of providing the good or service where there is no readily identifiable market price.

From Affiliates to APS:

- At a price not to exceed market price where a readily determinable market price for comparable services exists (as defined in section VI-B-2 above).
- At a price not to exceed fully loaded costs where a readily determinable market price does not exist.

3. Recording:

Charges for goods or services will be calculated by the entity providing the service. The entity receiving the goods or services may request that Pinnacle West audit the transactions. APS will record the fully loaded cost of any such goods or services provided by APS, and any corresponding revenues, below-the-line.

D. TRANSFER OF ASSETS & LIABILITIES

When specific assets or liabilities are identified for transfer between APS and Affiliates, an agreement must be formalized in writing covering the specific assets or liabilities to be transferred. All such agreements must be approved by an appropriate officer of Pinnacle West and each Affiliate and by the Pinnacle West Controller or designee. Copies of the agreements

must be provided to the Pinnacle West Controller or designee. Procedures for accounting and billing for the value of the assets or liabilities transferred shall be included in the agreement.

1. Identification:

Transfers of assets include transfers of tangible real or depreciable personal property and intangible property used in a trade or business.

Real property:

Includes, but is not limited to:

- Land
- Buildings
- Improvements
- Easements
- Other real property rights

Personal property:

Includes, but is not limited to:

- Automobiles
- Power-operated equipment
- Computer hardware
- Computer software or application software
- Furniture
- Materials and supplies

Intangible property:

Includes, but is not limited to:

- Copyrights
- Patent rights
- Royalty interests
- Licenses
- Trademarks
- Other proprietary information

Transfers of liabilities include, but are not limited to, accounts payable, notes payable, lease obligations, debt, pension and other post retirement benefits, deferred compensation and other items related to employees of APS and the Affiliates.

2. Valuation:

Transfers of assets and liabilities between APS and its Affiliates will be at net book value as of the date of the transfer in accordance with Generally Accepted Accounting Principles and SEC requirements.

3. Recording:

Transfers of assets or liabilities will be recorded through a direct charge.

VII. INTERCOMPANY BILLINGS AND REIMBURSEMENTS

A. GENERAL

Billing for inter-company transactions shall be issued on a timely basis, at least monthly, for goods or services and at the time of transfer for assets or liabilities. Sufficient detail will be provided to ensure an adequate audit trail and enable prompt reimbursement from the recipient of the assets, liabilities, goods, or services.

B. INTER-COMPANY BILLINGS AND PAYMENTS

Inter-company billing issued for transfers of assets, liabilities, goods, or services will be accompanied by or referenced to appropriate supporting documents. Allocations will be based upon methods set forth in these policies or applicable references. Such computations must be documented in order to facilitate verification of the costs of transferred assets, liabilities, goods, or services. Costs incurred on behalf of APS or its Affiliates shall be accumulated, priced, and billed no later than the end of the following month to enable timely payment.

Payments, or formal arrangement for payment, for assets, liabilities, goods, or services received from APS or an Affiliate shall be made no later than 30 days after receipt of an invoice. Inter-company billing and payments shall be adequately documented so that an audit trail exists to facilitate verification of the accuracy and completeness of all billings and reimbursements.

C. RECORDING

The receipt of an inter-company billing shall promptly be recorded in the accounting records of APS or the Affiliate receiving the billing. Disputes shall not preclude recording of the billing. Adjustments to prices, if necessary, will be proposed and resolved as soon as practicable after the billing is recorded.

VIII. INCOME AND OTHER TAXES

Federal and State tax liabilities and benefits and allocations will be handled in accordance with the Tax Allocation Agreement in place between Pinnacle West and its Affiliates.

IX. AUDITS

These Affiliate Accounting Policies will be subject to periodic audits performed by the internal auditors of Pinnacle West.