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Arizona Corporation Commission

DOCKET NO.

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BEFORE THE

ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION

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DIRECT TESTIMONY OF JACK E. DAVIS

On Behalf of

Arizona Public Service Company

Docket No. E-01345A-98-0473

Docket No. E-01345A-97-0773

Docket No. RE-00000C-94-0165

January 21, 2000

TABLE OF CONTENTS

	Page
I. INTRODUCTION	1
II. BACKGROUND AND OVERVIEW OF APS' PROPOSED CODE OF CONDUCT	3
III. IMPLEMENTING APS' CODE OF CONDUCT	9
IV. COMMENTS ON STAFF'S AND OTHER PARTIES' CODE OF CONDUCT PROPOSALS.....	12
V. CONCLUSION.....	18
SCHEDULE JED-1..... STATEMENT OF WITNESS QUALIFICATIONS	
SCHEDULE JED-2.....APS' FINAL PROPOSED CODE OF CONDUCT	
SCHEDULE JED-3..... APS' POLICIES AND PROCEDURES	

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DIRECT TESTIMONY OF JACK E. DAVIS

(Docket Nos. E-01345A-98-0473, et al.)

I. INTRODUCTION

5 **1.Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?**

6 1.A. My name is Jack E. Davis, and my business address is 400 North Fifth Street,
7
8 Phoenix, Arizona 85004

9 **2.Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

10 2.A. I am President of Energy Delivery and Sales for Arizona Public Service Company
11
12 (“APS” or “Company”). My educational, professional qualifications and
13 experience are set forth in Schedule JED-1, which is attached to my testimony.
14

15 **3.Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
16 **PROCEEDING?**

17 3.A. Last October, the Arizona Corporation Commission (“Commission”) adopted the
18 final Electric Competition Rules, A.A.C. R14-2-1601, *et seq.* (“Rules”), and
19 approved APS’ Settlement Agreement on Electric Competition-related issues
20 (“Settlement Agreement”). The Rules were adopted in Decision No. 61969
21 (September 29, 1999) and the Settlement Agreement was approved in Decision No.
22 61973 (October 6, 1999).
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1 Rule R14-2-1616 requires each Affected Utility to propose a code of
2 conduct that addresses nine subject areas within 90 days of the adoption of the
3 Rules. APS thereafter submitted a Code of Conduct on October 28, 1999. APS
4 then filed its final proposed code of conduct ("Code of Conduct") on January 5,
5 2000 after receiving and considering numerous comments from Staff and several
6 other interested parties. A copy of APS' final proposed Code of Conduct can be
7 found as Attachment JED-2 to my testimony.
8
9

10 To assist the parties and the Hearing Officer in considering the Code of
11 Conduct, my testimony will first provide an overview of APS' Code of Conduct
12 and the background behind its adoption. I will then briefly discuss APS' Policies
13 and Procedures for the Code of Conduct ("Policies and Procedures"), which were
14 filed with the Commission on January 12, 2000. The Policies and Procedures show
15 how APS will implement specific provisions of the Code of Conduct. Finally, I
16 will address some of the comments and the alternative proposed code of conduct
17 submitted by Staff's outside consultant, Ms. Gretchen McClain, as well as some
18 comments submitted by other parties. Although APS did not adopt all the
19 recommendations regarding its Code of Conduct from Staff and other parties, I
20 believe that our proposed Code of Conduct meets both the letter and the spirit of
21 Rule R14-2-1616 and, of equal importance, will be effective with and clear to our
22 employees.
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1 Finally, I would hasten to add that due to the number of suggestions and
2 recommendations that APS received on its Code of Conduct in the various rounds
3 of comments, I have not addressed every issue raised by every party. By not
4 addressing a specific comment of a specific party, neither I nor APS are necessarily
5 indicating agreement with the comment.
6

7
8 **II. BACKGROUND AND OVERVIEW OF**
9 **APS' PROPOSED CODE OF CONDUCT**

10 **4.Q. PLEASE DESCRIBE THE PROCEDURAL BACKGROUND OF APS'**
11 **PROPOSED CODE OF CONDUCT.**

12 4.A. First, I would point out that as part of the Settlement Agreement APS has had an
13 Interim Code of Conduct in effect since August 1999 to govern APS' relationship
14 with its competitive retail electric affiliate, APS Energy Services. A revised
15 version of that Interim Code of Conduct was filed with the Commission and served
16 on all parties to the APS Settlement Docket on October 28, 1999, as required by
17 Decision No. 61973.
18

19
20 Subsequently, the Hearing Division's November 9, 1999 Procedural Order
21 invited interested parties to file comments with APS regarding its original proposed
22 Code of Conduct. APS received comments from Staff, New West Energy
23 ("NWE"), Enron Corp. ("Enron"), and the Arizona Transmission Dependent
24 Utilities Group ("ATDUG"). Staff filed its comments as direct testimony, and their
25
26

1 consultant proposed an alternative code of conduct. NWE supported APS'
2 proposed Code of Conduct without modification.
3

4 APS considered all of the suggestions on revising its original proposed Code
5 of Conduct. Ultimately, several suggestions were adopted in the final proposed
6 Code of Conduct filed with the Commission on January 5, 2000. A brief
7 explanation of why APS accepted or rejected certain comments appears in the
8 January 5, 2000 cover letter transmitting the final proposed Code of Conduct.
9

10 On January 18, 2000, Staff filed comments (characterized as rebuttal
11 testimony from its consultant) and a revised alternative code of conduct. The only
12 other party that filed comments on this date was ATDUG.
13

14
15 **5.Q. WHAT UNDERLYING POLICIES DID APS SEEK TO ADDRESS IN ITS**
16 **CODE OF CONDUCT?**

17 5.A. In addition to covering the nine areas described in Rule R14-2-1616, APS' Code of
18 Conduct was drafted to address two core issues: cross-subsidization by APS'
19 customers and anticompetitive discrimination. APS agrees that it is improper for a
20 regulated electric distribution company to cross-subsidize; that is to include a
21 competitive retail electric affiliate's costs in APS' regulated rates. Similarly, it
22 would be improper for APS to discriminate in an anticompetitive fashion by, for
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1 example, providing only APS Energy Services with marketing leads obtained
2 through APS' role as a provider of distribution service.
3

4 Cross-subsidization and anticompetitive discrimination are legitimate areas
5 of concern that should be addressed in a code of conduct, and APS has, in fact,
6 addressed these issues in its Code of Conduct.
7

8 In addition to addressing these core policies, a well-drafted code of conduct
9 institutionalizes rules and policies that prevent improper anticompetitive conduct.
10 Written rules and policies are a tool to help guide our employees and corporate
11 leadership to make the right decisions. Indeed, for these same reasons, APS has
12 had for many years a formal Corporate Ethics Policy that provides written ethical
13 and standards of conduct guidelines for all Pinnacle West personnel. We have thus
14 tried to draft the Code of Conduct, as well as implementing Policies and
15 Procedures, in a manner and style that will be clear and effective with our
16 employees.
17
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19

20 **6.Q. TURNING TO THE CORE ISSUES YOU JUST IDENTIFIED, HOW DOES**
21 **APS' CODE OF CONDUCT ADDRESS CROSS-SUBSIDIZATION?**

22 6.A. First, Section 3.1 of the Code of Conduct contains a directive that APS will not
23 subsidize its competitive retail electric affiliates through improper charges to APS
24 customers. That directive is then elaborated upon, with Section 3.2 requiring APS
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1 to segregate costs and revenues and Section 3.3 requiring both APS and a
2 competitive retail electric affiliate to allow the Commission to inspect books and
3 records to determine compliance with the Code of Conduct.
4

5 In addition to Section 3, the Code of Conduct requires structural separations
6 between APS and affiliates in Section 4. Those structural separations—which also
7 protect against anticompetitive discrimination—help make APS’ cost allocation
8 process more effective. The physical separation of APS and APS Energy Services
9 ensures, for example, that an employee of APS Energy Services doesn’t
10 inadvertently use an APS photocopier to copy a document for APS Energy
11 Services, make calls on APS phones, etc.
12
13

14 Section 6 of the Code of Conduct contains specific pricing provisions to
15 restrict cross-subsidization. If an affiliate wishes to purchase goods or services
16 from APS, it must pay the full tariffed rate applicable to all purchasers of the good
17 or service. If there is no tariffed rate, the affiliate must pay the market price. If
18 there is no readily identifiable or ascertainable market price, the affiliate must pay
19 no less than the Company’s fully allocated cost of providing the good or service.
20
21 On the other hand, if APS wishes to purchase a good or service from an affiliate, it
22 cannot pay more than the market price or, if no market price is readily identifiable
23 or ascertainable, it must pay no more than the fully allocated cost of providing the
24 good or service.
25
26

1 Finally, I believe that it is important to recognize that the rate moratorium
2 that resulted from the APS Settlement Agreement also protects against cross-
3 subsidization. Because APS is giving rate reductions between now and 2004, we
4 cannot increase rates to subsidize a competitive retail electric affiliate.
5

6 **7.Q. HOW DOES APS' CODE OF CONDUCT ADDRESS ANTICOMPETITIVE**
7 **DISCRIMINATION?**
8

9 7.A. Section 4 of the Code of Conduct requires physical separation between APS and its
10 competitive retail electric affiliates. Such separation necessarily reduces the
11 opportunities for information to be improperly transferred between APS and an
12 affiliate. Additionally, we have adopted Enron's suggestion that if computer,
13 telecommunications, or information systems are shared with an affiliate, there must
14 be security safeguards to protect against the improper disclosure of information.
15

16
17 Additionally, Sections 4.1.7 and 4.2 require that requests for regulated
18 services be handled the same way, regardless of whether the requestor is APS
19 Energy Services or an unaffiliated ESP. APS is committed to administering its
20 tariffs and providing regulated services in a completely impartial manner.
21

22 Section 5 of the Code of Conduct addresses information sharing.
23 Essentially, there are three types of competitive information that must be
24 addressed: (1) system information (such as transmission availability), (2) customer
25
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1 information, and (3) supplier information. APS will provide system information to
2 all parties equally and at the same time—much of it by simply posting on APS’
3 OASIS when released. There will be no secret channels passing such information
4 to APS’ competitive retail electric affiliates. Customer information will not be
5 released to any ESP, including APS Energy Service, unless the customer has
6 specifically authorized the release of the information in writing. Similarly, APS
7 will not share—with APS Energy Services or any other ESP—supplier information
8 regarding a specific ESP, such as specific scheduling information, etc.
9
10

11 **8.Q. WHAT OTHER PROTECTIONS ARE INCLUDED IN APS’ CODE OF**
12 **CONDUCT?**
13

14 8.A. In addition to protections for cross-subsidization and discrimination, Section 4.3
15 contains detailed provisions to address advertising and marketing. These
16 provisions ensure that customers are informed of the nature of APS Energy
17 Services’ relationship to APS, and will not be confused about this relationship.
18

19 Section 7 describes how APS will provide its employees with access to the
20 Code of Conduct and Policies and Procedures, as well as the training program that
21 we have developed. This section also addresses compliance with the Code of
22 Conduct.
23

24 Finally, as suggested by Staff, Section 9 was added to explicitly address
25 dispute resolution under Rule R14-2-212. Additionally, for internal complaints,
26

1 APS has expanded its former "Employee Concerns Line" to provide an avenue for
2 our employees to seek assistance on Code of Conduct concerns and to report
3 violations, in addition to covering the health and welfare matters that were
4 previously available through that system.
5

6 **III. IMPLEMENTING APS' CODE OF CONDUCT**

7 **9.Q. WAS APS' PROPOSED CODE OF CONDUCT INTENDED TO BE A ONE**
8 **HUNDRED PERCENT SELF-CONTAINED, SELF-IMPLEMENTING**
9 **DOCUMENT?**
10

11 9.A. No. Just as the enactment of legislation does not mean there is no need for
12 implementing agency regulations or other interpretive agency documents, both
13 internal and external, it was always contemplated and intended that APS have
14 policy and procedure documents. These documents are important to Company
15 employees and management, as well as regulators and other affected parties, to
16 both understand and implement the more general Code of Conduct provisions.
17 These could also be of assistance in measuring our compliance with such
18 provisions.
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1 **10.Q. COULD YOU BRIEFLY DESCRIBE THESE POLICIES AND**
2 **PROCEDURES?**

3 10.A. Yes. The policies and procedure documents submitted to Staff on January 12th
4 were divided into nine topics corresponding to sections of the Company's final
5 proposed Code of Conduct:
6

- 7 1. APS/Affiliate Accounting (Code of Conduct Sections 3 and 6);
- 8 2. Physical Separation of Entities (Code of Conduct Section 4);
- 9 3. Shared Officers and Directors (Code of Conduct Section 4);
- 10 4. Contracting for Services (Code of Conduct Section 4);
- 11 5. ESP Contacts and Requests for Service (Code of Conduct Section 4);
- 12 6. Joint Promotion, Sales and Advertising (Code of Conduct Section 4);
- 13 7. Access to Information (Code of Conduct Section 5);
- 14 8. Code of Conduct Training (Code of Conduct Section 7); and
- 15 9. Code of Conduct Complaint Resolution (Code of Conduct Section 9).

16
17
18 As you can see, not every Section of the proposed final Code of Conduct
19 has an associated policy or procedure document. Section 1 of the Code of Conduct
20 contains only definitions. To the extent such definitions are important to
21 understanding how a specific policy or procedure should be implemented (e.g., the
22 Affiliate Accounting Procedures), they are included as part of the implementing
23 document itself. Sections 2 and 8 of the Code of Conduct are, in the Company's
24
25
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1 opinion, self-explanatory and do not need any further guidelines for their
2 implementation. The same is true of certain specific provisions of Section 4.
3

4 **11.Q. ARE THESE POLICIES AND PROCEDURES SUBJECT TO FURTHER**
5 **CHANGE?**

6 11.A. Yes. They will undoubtedly have to be modified and additional detail will have to
7 be added depending both on the final Commission-approved Code of Conduct and,
8 more importantly, on our actual subsequent experience. No matter how specific
9 one makes these kinds of policies and procedures, there will be factual instances
10 where their application in practice will be unclear. No matter how generalized they
11 are, there will be factual instances that do not fit within any general rule. No
12 matter how effective they appear on paper, there will be factual instances where the
13 policies and procedures are ineffective in implementing the intent of the Code of
14 Conduct. In all these cases, the policies and procedures will have to be changed or
15 supplemented in some respect.
16
17
18

19 **12.Q. ARE YOU NOW ASKING THE COMMISSION TO APPROVE THE**
20 **POLICIES AND PROCEDURES FILED ON JANUARY 12, 2000?**
21

22 12.A. No. Such approval might imply that APS would also require Commission approval
23 to modify its Policies and Procedures in the types of situations described above.
24 The Company must have the ability to make these necessary changes without the
25 requirement of seeking formal Commission approval. Additionally, while it may
26

1 be appropriate for the Director of the Utilities Division to approve the initial
2 Policies and Procedures, and it may be appropriate for APS' subsequent
3 modifications to be provided to the Director, modifications to the Policies and
4 Procedures should not be subject to a formal approval process by the Director.
5

6 **IV. COMMENTS ON STAFF'S AND OTHER PARTIES'**
7 **CODE OF CONDUCT PROPOSALS**

8
9 **13.Q DOES APS AGREE WITH STAFF'S DISCUSSION ON JOINT SUPPORT**
10 **OFFICERS AND DIRECTORS?**

11 13.A. Yes. After Staff filed Ms. McClain's Direct Testimony, representatives from APS
12 met with Staff and discussed Staff's concerns on this issue. As a result, APS was
13 able to agree to restrictions on common officers and directors that I believe address
14 valid concerns about cross-subsidization and improper information sharing,
15 without interfering with legitimate corporate governance issues unrelated to the
16 Code of Conduct.
17

18 **14.Q. IN HER DIRECT TESTIMONY, STAFF'S CONSULTANT ARGUED THAT**
19 **ALLOWING AN AFFILIATE TO CONTRACT FOR SERVICES FROM AN**
20 **APS EMPLOYEE EFFECTIVELY CONSTITUTES JOINT**
21 **EMPLOYMENT. DO YOU AGREE?**
22

23 14.A. No. APS' position is best illustrated by an example. APS routinely contracts for
24 services with outside vendors. If, for example, APS contracts to have an engineer
25 from XYZ Software write and install a software patch on an APS system, that
26

1 engineer does not thereby become a joint employee of APS and XYZ Software.
2 Rather, the engineer is an employee of XYZ Software only. There is no
3 prohibition in the Rules on APS contracting with an affiliate for services. Indeed,
4 even Staff's proposed code of conduct recognizes that APS and its affiliates may
5 provide services to each other, as long as the pricing guidelines are followed.
6

7
8 Moreover, in its Policies and Procedures, APS has limited the ability for it
9 and its affiliates to contract for such services. These procedures were intentionally
10 drafted to prohibit "matrixing"—where an employee is assigned to an affiliate for
11 an indefinite period with an undefined scope of work but remains, for all practical
12 purposes, an APS employee. Under APS' Code of Conduct, the person providing
13 the services must have a recognized expertise needed for a project that has a
14 specified scope and a finite duration. The procedures also require personnel
15 involved in providing these services to formally sign a confidentiality/non-
16 disclosure agreement.
17
18

19 **15.Q. STAFF'S CONSULTANT ALSO REFERS TO "APS' COMPETITIVE**
20 **ACTIVITIES" AND APPEARS TO SUGGEST THAT APS MUST ADOPT**
21 **VARIOUS INTRA-COMPANY SEPARATIONS. DO YOU HAVE ANY**
22 **COMMENTS ON THESE REFERENCES?**
23

24 15.A. First let me say that I am not particularly clear on what Ms. McClain means by
25 "APS' competitive activities." Under Rule R14-2-1615, all Competitive Services
26

1 as defined by the Electric Competition Rules must be divested to an affiliate or an
2 unaffiliated third party. There are, however, a few services, such as providing
3 metering and meter reading services for load-profiled residential customers, that
4 are admittedly excluded from the separation requirements.
5

6 It appears that Section X.C of Staff's proposed Code of Conduct is meant to
7 prohibit, for example, APS from using the same employee to read both the
8 residential load-profiled meter of a direct access customer and Standard Offer
9 customers' meters on a particular meter route—even if the meter reading costs are
10 properly charged to such customers. If this is Staff's intent, APS will not be
11 willing to absorb the costs to segregate these intra-company services, or to
12 eliminate the very economies of scale that were the reason for excluding these
13 services from the definition of "Competitive Services" in the first place. Rather,
14 APS would not provide metering or meter reading services for residential load-
15 profiled customers because it could not justify providing these services from a
16 business standpoint. It may also foreclose APS from ever offering consolidated
17 billing, if Staff considers such billing to be a "Permitted Competitive Service"
18 requiring structural separation and burdensome reporting.
19
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23 As to "Interim Competitive Services," APS is not now, and has no intention
24 of, providing such services, as defined by Ms. McClain, during the transition prior
25
26

1 to December 31, 2002. All competitive retail electric services will be provided
2 through an affiliate.
3

4 **16.Q. DO YOU AGREE WITH STAFF'S PROVISIONS IN SECTION XI OF**
5 **STAFF'S REVISED CODE OF CONDUCT, REGARDING TRANSFER**
6 **PRICING FOR NON-TARIFFED GOODS AND SERVICES?**
7

8 16.A. No, I do not. Such a restriction would unfairly deny APS Energy Services the
9 opportunity to purchase goods and services from a sister corporation, and would
10 prevent APS customers from benefiting from transactions that may be below fully
11 allocated cost but still above incremental cost.
12

13 **17.Q. ENRON CLAIMS THAT APS' CODE OF CONDUCT DOES NOT**
14 **ADEQUATELY ADDRESS ITS CONTINUED OWNERSHIP OF**
15 **GENERATION ASSETS. DO YOU AGREE?**
16

17 17.A. No. As Staff acknowledged in its Rebuttal Testimony, the Code of Conduct is
18 intended to address retail electric competition. APS generation (pre-divestiture)
19 will be used only for: (1) Standard Offer Service, a defined "noncompetitive
20 service" under the Electric Competition Rules; and (2) wholesale transactions.
21 APS is not selling competitive generation at retail, and will not sell competitive
22 generation at retail, during the transition period. Thus, the numerous questions that
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1 Enron poses at page 5 of its testimony are completely unrelated to retail electric
2 competition or, conversely, are subject to APS' FERC Code of Conduct.
3

4 For example, Enron questions how APS will "dispose of excess [generation]
5 capacity and how will it treat the revenues therefrom?" APS will sell its excess
6 generation capacity on the open market and will—as it has done for the more than
7 25 years I have worked for the Company—account for such sales according to the
8 requirements of FERC's and this Commission's Uniform System of Accounts.
9 APS' sales of generation at the wholesale level are by no means a new
10 development brought about by the Electric Competition Rules. Moreover, APS'
11 rate increase moratorium, along with annual fixed decreases, are in place
12 irrespective of the level of or price for any wholesale sales.
13
14

15 Enron also suggests that the Commission should require that APS sell
16 "excess" generation to the highest bidder. That is in fact our goal.
17
18

19 Finally, Enron's concerns over how APS will manage its transmission and
20 distribution capacity are misplaced given the subject matter of this proceeding.
21 Those concerns are not code of conduct issues. APS' FERC-imposed OATT and
22 OASIS requirements address the management of transmission, and the Electric
23 Competition Rules require APS to ensure that there is adequate distribution
24 capacity to serve its customers.
25
26

1 **18.Q. DO YOU AGREE WITH ENRON THAT THE DISCLOSURE**
2 **REQUIREMENTS FOR PROMOTIONAL OR ADVERTISING**
3 **MATERIALS SHOULD EXTEND BEYOND WRITTEN MATERIALS.**
4

5 18.A. No. What I think of as the utility equivalent of "Miranda" warnings on written
6 promotional and advertising material are sufficient to prevent customer confusion.
7 Requiring an APS Energy Services employee to provide Enron's 50-word
8 "Miranda" warning prior to speaking with any potential customer or even before
9 speaking, in say an Open Meeting, is unreasonable. It certainly goes beyond the
10 "guidelines" that are required by Rule R14-2-1616(B)(4).
11

12
13 **19.Q. DO YOU AGREE WITH THE RECOMMENDATION OF STAFF'S**
14 **CONSULTANT THAT APS SHOULD SUBMIT ANNUAL REPORTS ON**
15 **ITS COST ALLOCATIONS?**

16 19.A. No. The Electric Competition Rules and APS' Code of Conduct give the
17 Commission the authority to inspect the books and records of APS and its
18 competitive retail electric affiliates. There is no evidence that this authority,
19 together with the existing reports required of APS and its affiliates, will be
20 *inadequate to provide sufficient information for the Commission to determine*
21 *compliance with the Code of Conduct. The Commission should not impose*
22 *burdensome, routine reporting requirements unless and until they are necessary.*
23
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1 V. CONCLUSION

2 **20.Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

3 20.A. APS has developed a Code of Conduct, and implementing Policies and Procedures,
4 that complies with the nine requirements for codes of conduct under Rule R14-2-
5 1616(B). We appreciate the hard work of Staff and the intervenors to this
6 proceeding who recommended modifications to APS' Code of Conduct. I can
7 assure you that each recommendation was considered by the Company, and I
8 believe that an improved Code of Conduct resulted from that process.
9
10

11 APS does not, however, believe that either it or the Commission should
12 accept recommendations to modify the proposed Code of Conduct in a way that
13 would impose conditions beyond those in the Electric Competition Rules. The
14 intra-company separations for "Permitted Competitive Services" proposed by Staff
15 do that, as do proposals for required reporting and outside audits.
16
17

18 APS' proposed Code of Conduct submitted on January 5, 2000 and its
19 implementing Policies and Procedures will effectively address legitimate concerns
20 of cross-subsidization and anticompetitive discrimination involving APS and its
21 competitive retail electric affiliates. The proposed Code of Conduct meets both the
22 substance and the intent of Rule R14-2-1616, without imposing unreasonable
23 burdens and obligations that would really do no more than improperly subsidize
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1 new market entrants at the expense of the Company, its customers, and ultimately
2 the consumers in this state.

3

4 **21.Q. WHAT IS APS' INTENT REGARDING ITS CODE OF CONDUCT?**

5 21.A. Above all else, APS will continue to do business in a fair and honest manner. We
6 will meet the letter, spirit, and intent of the Code of Conduct. I ask the
7 Commission and new market entrants not to presume—as do some of the
8 comments and recommendations filed in this proceeding—that APS will act
9 unethically or anticompetitively in a restructured electric industry. Our history of
10 service in this state warrants precisely the opposite presumption.

12

13 **22.Q. DOES THIS CONCLUDE YOUR DIRECT WRITTEN TESTIMONY?**

14

15 22.A. Yes.

16

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STATEMENT OF WITNESS QUALIFICATIONS

Jack E. Davis is President of Energy Delivery and Sales for Arizona Public Service Company. As President of Energy Delivery and Sales, Mr. Davis has responsibility for Bulk Power Trading, Transmission Planning and Operations, Customer Service, Economic Development, and Pricing and Regulation.

Mr. Davis graduated from New Mexico State University in 1969 with a Bachelor of Science Degree in Medical Technology and in 1973 with a Bachelor of Science in Electrical Engineering. He joined Arizona Public Service Company that same year and has held various supervisory and managerial positions in both the System Planning and Power Contracts and Systems Operations Departments. In 1990, Mr. Davis was named Director of System Development and Power Operation and thereafter promoted to Vice-President of Generation and Transmission in 1993. In October 1996, he was named Executive Vice President of Commercial Operations.

Mr. Davis is the Past President of the Western Energy Supply and Transmission, Chairman of the Western Systems Coordinating Council (WSCC), a member of the WSCC Board of Trustees, and (past chairman of the WSCC Regional Planning Policy Committee), a member of the National Electric Reliability Council Board of Trustees, and past President of the Western Systems Power Pool. Additionally, he is a registered professional electrical engineer in the State of Arizona.

Attachment JED-2

Code of Conduct

ARIZONA PUBLIC SERVICE COMPANY

Code of Conduct

Arizona Public Service Company ("APS") is committed to establishing standards of conduct that will produce confidence in the integrity of the competitive retail electric market and that will be consistent with the requirements of the Electric Competition Rules.

The following Code of Conduct shall apply to APS and, where indicated, its Affiliates.

1 Definitions

- 1.1 "ACC" means the Arizona Corporation Commission.
- 1.2 "Affiliate Interest Rules" means A.A.C. R14-2-801, et. seq.
- 1.3 "APS" means Arizona Public Service Company in its capacity of providing Distribution Service and any other electric services permitted by law.
- 1.4 "Competitive Electric Affiliate" means a business enterprise related to APS in the manner described in A.A.C. R14-2-801 (1) that is also an Electric Service Provider; hereinafter referred to as "Affiliate" or "Affiliates".
- 1.5 "Distribution Service" means those services described in A.A.C. R14-2-1601 (14), i.e., "the delivery of electricity to a retail consumer through wires, transformers, and other devices that are not classified as transmission services subject to the jurisdiction of the Federal Energy Regulatory Commission."
- 1.6 "Electric Competition Rules" means A.A.C. R14-2-1601, et. seq.
- 1.7 "Electric Service Provider" or "ESP" means a company supplying, marketing, or brokering at retail competitive electric services pursuant to a Certificate of Convenience and Necessity. This term has the same definition as in A.A.C. R14-2-1601 (16).

2 *General*

- 2.1 All employees and authorized agents of APS shall conduct their activities in compliance with the requirements of this Code of Conduct.
- 2.2 Failure to conduct activities in compliance with this Code of Conduct will subject the employee or agent to disciplinary actions described in Section 7.
- 2.3 APS shall adopt and follow written policies and procedures regarding the implementation of this Code of Conduct.

3 *Financial*

- 3.1 *Subsidization.* APS shall not subsidize the competitive electric services provided by an Affiliate through any charge for goods or services which is not in conformance with Section 6.
- 3.2 *Segregation.* Costs and revenues of APS shall be segregated from costs and revenues of Affiliates in a manner sufficient to ensure compliance with Section 3.1.
- 3.3 *Books and Records.* APS shall maintain its books of account and records separately from those of its Affiliates. As a precondition to transacting any business with APS, Affiliate books and records must be made available for inspection by the ACC to the extent reasonably necessary to determine compliance with this Code of Conduct.

4 *Separation of Functions*

4.1 *Operations*

- 4.1.1 APS shall exist as a separate corporate entity from any Affiliate.
- 4.1.2 APS shall not use shared corporate support functions as a means to circumvent Section 5.
- 4.1.3 Nothing in this Code of Conduct shall prevent APS and an Affiliate from receiving shared services from Pinnacle West Capital Corporation. Such shared services and the assignment or allocation of costs therefor shall be as set forth in APS' Affiliate Accounting Policies and Procedures.

- 4.1.4 Shared telecommunication, computer and information systems shall be secured with appropriate security devices and procedures to protect against the disclosure of information in a manner inconsistent with this Code of Conduct.
- 4.1.5 Except as permitted by this Code of Conduct, APS shall not jointly employ the same employees as its Affiliates.
 - 4.1.5.1 For purposes of common oversight and governance, APS and its Affiliates may share one or more officers and directors. Officers and directors may be shared only where sufficient mechanisms are in place so that such sharing does not result in circumventing any of the Code of Conduct provisions. Officers and directors shall sign a statement annually that they understand the Code of Conduct and the attendant consequences for violations thereof.
- 4.1.6 An Affiliate may contract for services from APS when a written service agreement is executed in accordance with established policies and procedures and when the charges for such services comply with Section 6.
- 4.1.7 Requests from Affiliates and non-affiliated ESPs and their customers for ACC-regulated services provided by APS shall be processed on a non-discriminatory, first come, first served-basis and in accordance with established policies and procedures and also as set forth in Schedule 10 of APS' ACC-approved tariffs.

4.2 *Administering Tariffs.*

- 4.2.1 Administration and enforcement of all ACC-approved tariffs for APS, including terms and conditions of service, shall be conducted solely by employees and authorized agents of APS.
- 4.2.2 With respect to the terms and conditions of providing Distribution Services subject to ACC approval (including price, curtailments, scheduling and priority), APS shall not provide its Affiliates, or the customers of its Affiliates, any preferential treatment over non-affiliated ESPs or their customers as a result of such status as an Affiliate or customer of an Affiliate.
- 4.2.3 If a tariff provision allows for discretion in its application, APS shall apply that provision in a non-discriminatory manner between an Affiliate and all other market participants and their respective customers.

4.2.4 APS shall not condition or otherwise tie any non-competitive electric service it provides nor the availability of discounts of rates or other charges or fees, rebates, or waivers of terms and conditions of such service to a Distribution Service customer taking any goods or services from an Affiliate.

4.2.5 Prior to the divestiture of APS generation pursuant to ACC Decision No. 61973 (October 6, 1999), APS generation shall not be sold by APS on a discounted basis to Standard Offer customers without the express permission of the ACC.

4.3 *Promotion, Sales and Advertising of Non-Distribution Services.*

4.3.1 APS shall not engage in any joint advertising, marketing or sales activity of any sort with an Affiliate.

4.3.2 APS shall not permit an Affiliate to use APS' name or logo in written promotional or advertising material unless the Affiliate discloses that: 1) the Affiliate is not the same company as APS and 2) customers do not have to buy the Affiliate's product in order to continue to receive Distribution Service at regulated rates from APS.

4.3.3 APS shall not promote, market, or sell an Affiliate's services for or on behalf of an Affiliate.

4.3.4 APS shall not state or imply in any advertising or customer communication that the provision of any Distribution Service, or the terms and conditions governing such services, are conditioned upon, related to or tied to the purchase of any other product or service from an Affiliate, or that APS is the same entity as such Affiliate.

4.3.5 APS shall not provide advice regarding an Affiliate to APS' customers nor state or imply that Distribution Service provided to an Affiliate's customer is safer or more reliable than those provided to a non-Affiliate or that an Affiliate's customers will receive preferential treatment from APS regarding their Distribution Services.

4.3.6 APS shall not provide an Affiliate with advertising space in any APS written customer communication (e.g., billing) unless access is made available to non-affiliated ESPs on the same terms and conditions.

4.3.7 APS shall inform customers who inquire about competitive services that a list of authorized ESPs is available from the ACC. APS may offer customers the ACC website address and telephone number or, upon request, may provide the customer with a copy of the current ACC list of authorized ESPs as shown on the ACC website at the time of the customer's inquiry.

5 Access to Information

5.1 *System Information.* APS shall provide Affiliates and non-Affiliates access to Distribution Service-specific information (including information about available distribution capability, transmission access and curtailments) under the same terms and conditions and in accordance with established policies and procedures.

5.2 *Customer Information.* Non-public customer-specific information shall not be provided by APS to an Affiliate unless release of such information is expressly authorized by the customer or the ACC or is otherwise permitted by law.

6 Transactions with Affiliates

6.1 *Accounting.* Transactions between APS and an Affiliate shall be accounted for in accordance with Generally Accepted Accounting Principles.

6.1.1 Accounting provisions for Affiliate transactions shall be governed by written policies and procedures that include but are not limited to general provisions, allocation methodologies for direct and indirect charges, goods or services produced, purchased or developed for sale and those not produced, purchased or developed for sale, transfer of assets, and inter-company billing and reimbursements.

6.2 *Purchase of Goods and Services from Affiliates.* APS shall not purchase goods and services from an Affiliate at a price that is above the market price of such goods and services or, where a market price for any particular good or service is not readily available, at a price that is above the Affiliate's fully allocated cost of providing the good or service.

6.3 *Sale of Goods and Services to Affiliates.* Goods and services sold by APS to an Affiliate shall be charged in accordance with any applicable tariff. Where a tariff is not applicable, such goods and services shall be

sold at the market price or where there is no readily identified market price, at the fully allocated cost of providing the good or service.

- 6.4 *Reporting Requirements.* Contracts pertaining to transactions between APS and an Affiliate as described in Sections 6.2 and 6.3 shall be provided to the ACC in compliance with the reporting requirements of the Affiliate Interest Rules.

7 Dissemination, Education and Compliance

- 7.1 *Employee Access to Code of Conduct.* Copies of this Code of Conduct and associated policies and procedures shall be provided to employees of APS and all Affiliates and those authorized agents of APS and all Affiliates that are likely to be engaged in activities subject to the Code of Conduct. A copy of the Code of Conduct and associated policies and procedures shall be maintained on Pinnacle West's Intranet.

- 7.2 *Employee Training.* Training on the provisions of the Code of Conduct and its implementation through associated policies and procedures, shall be provided to APS employees and authorized agents likely to be engaged in activities subject to the Code of Conduct.

- 7.3 *Compliance.*

- 7.3.1 Compliance with the Code of Conduct is mandatory. An APS employee's or agent's failure or refusal to abide by or to act according to such standards may subject the employee or agent to disciplinary action, up to and including discharge from employment or termination of the agent's relationship with APS.

- 7.3.2 Compliance with this Code of Conduct shall be administered as part of the Pinnacle West Business Practices program and in accordance with Pinnacle West Business Practices policies.

8 Modifications to the Code of Conduct

- 8.1 APS shall request modifications to this Code of Conduct by filing an application with the ACC. The application shall set forth the proposed modifications and supporting reasons.

9 *Dispute Resolution*

- 9.1 To the extent permitted by law, complaints concerning violations of this Code of Conduct shall be processed under the procedures established in A.A.C. R14-2-212.

Questions regarding this Code of Conduct should be directed to the Pinnacle West Business Practices Department.

ARIZONA PUBLIC SERVICE COMPANY

Code of Conduct

Arizona Public Service Company ("APS") is committed to establishing standards of conduct that will produce confidence in the integrity of the competitive retail electric market and that will be consistent with the requirements of the Electric Competition Rules.

The following Code of Conduct shall apply to APS and, where indicated, its Affiliates.

1 Definitions

1.1 ~~"Affiliate" or "Affiliates" means an Electric Service Provider related to APS in the manner described in A.A.C. R14-2-801 (1).~~ "ACC" means the Arizona Corporation Commission.

1.2 "Affiliate Interest Rules" means A.A.C. R14-2-801, et. seq.

1.3 "APS" means Arizona Public Service Company in its capacity of providing Distribution Service and any other electric services permitted by law.

~~1.3 "Commission" means the Arizona Corporation Commission.~~

1.4 ~~"Electric Competition Rules" means A.A.C. R14-2-1601 et. seq., as set forth in Decision No. 61968 (September 20, 1999).~~ "Competitive Electric Affiliate" means a business enterprise related to APS in the manner described in A.A.C. R14-2-801 (1) that is also an Electric Service Provider; hereinafter referred to as "Affiliate" or "Affiliates".

1.5 "Distribution Service" means those services described in A.A.C. R14-2-1601 (14), i.e., "the delivery of electricity to a retail consumer through wires, transformers, and other devices that are not classified as transmission services subject to the jurisdiction of the Federal Energy Regulatory Commission."

1.6 "Electric Competition Rules" means A.A.C. R14-2-1601, et. seq.

~~1.7~~ "Electric Service Provider" or "ESP" means a provider of company supplying, marketing, or brokering at retail competitive electric services.

~~as defined~~ services pursuant to a Certificate of Convenience and Necessity. This term has the same definition as in A.A.C. R14-2-1601 (16).

2 General

- 2.1 All employees and authorized agents of APS shall conduct their activities in compliance with the requirements of this Code of Conduct.
- 2.2 Failure to conduct activities in compliance with ~~the~~ this Code of Conduct will subject the employee or agent to disciplinary actions described in Section 7.
- 2.3 APS shall adopt and follow written policies and procedures regarding the implementation of this Code of Conduct.

3 Financial

- 3.1 *Subsidization.* APS shall not subsidize the competitive electric services provided by an Affiliate through any ~~rate or charge for non competitive electric services~~ charge for goods or services which is not in conformance with Section 6.
- 3.2 *Segregation.* Costs and revenues of APS ~~will~~ shall be segregated from costs and revenues of Affiliates in ~~the~~ a manner sufficient to ensure that ~~there is no subsidization of the business activities of Affiliates by any rate or charge for non competitive services of APS~~ compliance with Section 3.1.
- 3.3 *Books and Records.* APS ~~will~~ shall maintain its books of account and records separately from those of its Affiliates. As a precondition to transacting any business with APS, Affiliate books and records must be made available for inspection by the ~~Commission~~ ACC to the extent reasonably necessary to determine compliance with this Code of Conduct.

4 Separation of Functions

- 4.1 *Operations-*

4.1.1 ~~Except as otherwise permitted by law or in this Code of Conduct,~~ APS shall ~~operate~~exist as a separate corporate entity from any Affiliate.

4.1.2 APS shall not use shared corporate support functions as a means to circumvent Section 5, ~~transfer confidential customer information or create significant opportunities for cross subsidization of its competitive electric affiliates.~~

4.1.3 Nothing in this Code of Conduct shall prevent APS and an Affiliate from receiving shared services from Pinnacle West Capital Corporation. Such shared services and the assignment or allocation of costs therefor shall be as set forth in APS' Affiliate Accounting Policies and Procedures.

~~4.1.24.~~4.1.4 Shared telecommunication, computer and information systems shall be secured with appropriate security devices and procedures to protect against the disclosure of information in a manner inconsistent with this Code of Conduct.

4.1.5 Except as permitted by this Code of Conduct, APS ~~will~~shall not jointly employ the same employees as its Affiliates.

4.1.5.1 For purposes of common oversight and governance, APS and its Affiliates may share one or more officers and directors. Officers and directors may be shared only where sufficient mechanisms are in place so that such sharing does not result in circumventing any of the Code of Conduct provisions. Officers and directors shall sign a statement annually that they understand the Code of Conduct and the attendant consequences for violations thereof.~~Affiliate. However, to provide for joint corporate oversight, governance and support, this provision shall not prevent APS and any Affiliate from having common Directors or Officers. An Affiliate may also~~

4.1.6 An Affiliate may contract for services from APS as long as when a written service agreement is executed in accordance with established policies and procedures and when the charges for such services comply with Section 6~~of this Code of Conduct.~~

4.1.7 Requests from Affiliates and non-affiliated ESPs and their customers for ACC-regulated services provided by APS shall be processed on a ~~non-discriminatory basis~~non-discriminatory, first come, first served-basis and in accordance with established

policies and procedures and also as set forth in Schedule 10 of APS' ACC-approved tariffs.

4.2 *Administering Tariffs.*

4.2.1 Administration and enforcement of all ~~Commission approved~~ ACC-approved tariffs for APS, including terms and conditions of service, ~~will~~ shall be conducted solely by employees and authorized agents of APS.

4.2.2 With respect to the terms and conditions of providing Distribution Services subject to ACC approval (including price, curtailments, scheduling and priority), APS shall not provide its Affiliates, or the customers of its Affiliates, any preferential treatment over non-affiliated ESPs or their customers as a result of such status as an Affiliate or customer of an Affiliate.

4.2.3 If a tariff provision allows for discretion in its application, APS shall apply that provision in a non-discriminatory manner between an Affiliate and all other market participants and their respective customers.

4.2.4 APS shall not condition or otherwise tie any non-competitive electric service it provides nor the availability of discounts of rates or other charges or fees, rebates, or waivers of terms and conditions of ~~its~~ such service to ~~the~~ a Distribution Service customer taking ~~of~~ any goods or services from an Affiliate.

4.2.5 Prior to the divestiture of APS generation pursuant to ACC Decision No. 61973 (October 6, 1999), APS generation ~~will~~ shall not be sold by APS on a discounted basis to Standard Offer customers without the express permission of the ACC.

4.3 *Promotion, Sales and Advertising of Non-Distribution Services.*

4.3.1 APS shall not engage in any joint advertising, marketing or sales activity of any sort with an Affiliate.

~~4.3.1~~ 4.3.2 APS shall not permit an Affiliate to use APS' name or logo ~~shall not be used~~ in written promotional or advertising material ~~circulated by an Affiliate~~ unless the Affiliate discloses that: 1) the Affiliate is not the same company as APS and 2) customers do not have to buy the Affiliate's product in order to continue to receive Distribution Service at regulated rates from APS.

~~4.3.2 APS will not engage in joint advertising, marketing or sales with its Affiliate.~~

4.3.3 APS shall not promote, market, or sell an Affiliate's services for or on behalf of an Affiliate.

4.3.4 APS shall not state or imply in any advertising or customer communication that the provision of any Distribution Services, or the terms and conditions governing such services, are conditioned upon, related to or tied to the purchase of any other product or service from an Affiliate, or Affiliate that APS is the same entity as such Affiliate.

4.3.5 APS shall not ~~offer or~~ provide advice regarding an Affiliate to APS' customers nor state or imply that Distribution service Service provided to an Affiliate's customer is safer or more reliable than those provided to a non-Affiliate or that an Affiliate's customers will receive preferential treatment from APS regarding their Distribution Services.

4.3.6 APS shall not ~~offer or~~ provide an Affiliate with advertising space in any APS written customer communication (e.g., billing) unless access is provided to non-Affiliates made available to non-affiliated ESPs on the same terms and conditions.

4.3.7 APS shall inform customers who inquire about competitive services that a list of authorized ESPs is available from the ACC. APS may offer customers the ACC website address and telephone number or, upon request, may provide the customer with a copy of the current ACC list of authorized ESPs as shown on the ACC website at the time of the customer's inquiry.

5 Access to Information

5.1 *System Information.* APS shall provide ~~an Affiliate and non-Affiliate ESPs~~ Affiliates and non-Affiliates access to Distribution Service-specific information (including information about available distribution capability, transmission access and curtailments) ~~concurrently and~~ under the same terms and conditions. and in accordance with established policies and procedures.

5.2 *Customer Information.* Non-public customer-specific information ~~will~~ shall not be provided by APS to an Affiliate ~~or to a non-Affiliate~~ unless release of such information is expressly authorized by the customer or

the ~~Commission~~ ACC or is otherwise ~~authorized or required~~ permitted by law.

6 Transactions with Affiliates

6.1 *Accounting.* ~~Except where regulatory requirements provide otherwise, transactions~~ Transactions between APS and an Affiliate ~~will~~ shall be accounted for in accordance with Generally Accepted Accounting Principles.

6.1.1 Accounting provisions for Affiliate transactions shall be governed by written policies and procedures that include but are not limited to general provisions, allocation methodologies for direct and indirect charges, goods or services produced, purchased or developed for sale and those not produced, purchased or developed for sale, transfer of assets, and inter-company billing and reimbursements.

6.2 *Purchase of Goods and Services from Affiliates.* APS shall not purchase goods and services from an Affiliate at a price that is above the market price of such goods and services or, where a market price for any particular good or service is not readily available, at a price that is above the Affiliate's fully allocated cost of providing the good or service.

6.3 *Sale of Goods and Services to Affiliates.* Goods and services sold by APS to an Affiliate shall be charged in accordance with any applicable tariff. Where a tariff is not applicable, such goods and services shall be sold at the market price or where there is no readily identified market price, at the fully allocated cost of providing the good or service.

6.4 ~~*Policies and Procedures.* APS shall maintain, or cause to be maintained, written policies and procedures regarding the accounting and aggregation of costs as between APS and an Affiliate, which policies and procedures shall be made available to the Commission on request.~~ *Reporting Requirements.* Contracts pertaining to transactions between APS and an Affiliate as described in Sections 6.2 and 6.3 shall be provided to the ACC in compliance with the reporting requirements of the Affiliate Interest Rules.

7 Dissemination, Education and Compliance

7.1 *Employee Access to Code of Conduct.* Copies of this Code of Conduct ~~will~~ and associated policies and procedures shall be provided to

employees of APS and all Affiliates and those authorized agents of APS and all Affiliates that are likely to be engaged in activities subject to the Code of Conduct. A copy of the Code of Conduct ~~will and associated policies and procedures shall~~ be maintained on ~~the Company's electronic bulletin board known as Vista Public Folders-~~ Pinnacle West's Intranet.

7.2 *Employee Training.* Training on the provisions of the Code of Conduct and its implementation ~~will through associated policies and procedures,~~ shall be provided to APS employees and authorized agents likely to be engaged in activities subject to the Code of Conduct.

7.3 Compliance.

7.3.1 ~~Compliance.~~ Compliance with the Code of Conduct is mandatory. An APS employee's or agent's failure or refusal to abide by or to act according to such standards may subject the employee or agent to disciplinary action, up to and including discharge from employment or termination of the agent's relationship with APS.

7.3.2 ~~Questions regarding this Code of Conduct should be directed to the~~ Compliance with this Code of Conduct shall be administered as part of the Pinnacle West Business Practices program and in accordance with Pinnacle West Business Practices policies ~~Department, the will APS Standard of Conduct program.~~

8 Modifications to the Code of Conduct

8.1 APS shall request modifications to this Code of Conduct by filing an application with the ACC. The application shall set forth the proposed modifications and supporting reasons.

9 Dispute Resolution

9.1 To the extent permitted by law, complaints concerning violations of this Code of Conduct shall be processed under the procedures established in A.A.C. R14-2-212.

Questions regarding this Code of Conduct should be directed to the Pinnacle West Business Practices Department.

Attachment JED-3

Policies and Procedures



THE POWER TO MAKE IT HAPPEN™

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.



THE POWER TO MAKE IT HAPPEN™

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.



THE POWER TO MAKE IT HAPPEN™

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.



THE POWER TO MAKE IT HAPPEN™

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.



THE POWER TO MAKE IT HAPPEN™

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.



THE POWER TO MAKE IT HAPPEN™

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, Troublemens 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.