ADOBE SYSTEMS INC
Form 8-K
April 11, 2008

# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

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# FORM 8-K

**CURRENT REPORT**

**Pursuant to Section 13 or 15(d) of the**
**Securities Exchange Act of 1934**

Date of Report (date of earliest event reported): **April 11, 2008**

# Adobe Systems Incorporated

(Exact name of Registrant as specified in its charter)

| | | |
|---|---|---|
| **Delaware** | **0-15175** | **77-0019522** |
| (State or other jurisdiction of incorporation) | (Commission File Number) | (I.R.S. Employer Identification No.) |

**345 Park Avenue**
**San Jose, California 95110-2704**
(Address of principal executive offices and zip code)

Registrant s telephone number, including area code: **(408) 536-6000**

**Not Applicable**

(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

**Item 5.02 Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers.**

**(e)** ***Amendment and Restatement of the Adobe Systems Incorporated 2003 Equity Incentive Plan***

At the Annual Meeting of Stockholders held on April 9, 2008, the stockholders of Adobe Systems Incorporated (the Company ) approved an amendment and restatement of the Company s 2003 Equity Incentive Plan (the 2003 Amended Plan ), which amendment and restatement had previously been approved by the Company s Board of Directors in January 2008, subject to stockholder approval.

The material amendments to the 2003 Amended Plan include:

- Concurrent termination of the Company s existing 1996 Outside Directors Stock Option Plan (the Director Plan ) and the expansion of the eligible class of participants under the 2003 Amended Plan to include non-employee directors;
- The increase of the available share reserve by 15,000,000 shares of the Company s common stock, as well as the inclusion of 785,000 shares of the Company s common stock that remained available for future issuance under the Director Plan; and
- The increase to the Company s existing fungible share reserve ratio so that the number of shares of stock available for issuance under the 2003 Amended Plan will be reduced (i) by one share for each share granted pursuant to stock options or stock appreciation rights awarded under the 2003 Amended Plan, and (ii) by two and four-tenths shares for each share granted pursuant to all other types of awards awarded under the 2003 Amended Plan.

The foregoing summary of the amendment and restatement of the 2003 Amended Plan is qualified in its entirety by the text of the 2003 Amended Plan, which is attached as Appendix A to the Company s definitive proxy statement on Schedule 14A filed with the Securities and Exchange Commission on February 27, 2008 and is hereby incorporated by reference herein.

**Item 9.01 Financial Statements and Exhibits.**

**(d) Exhibits**

| Exhibit | | Incorporated by Reference | | |
|---|---|---|---|---|
| Number | Exhibit Description | Form | Date | Number |
| 10.1 | 2003 Equity Incentive Plan, as amended and restated | DEF 14A | 2/27/08 | Appendix A |

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

| | | |
|---|---|---|
| | ADOBE SYSTEMS INCORPORATED | |
| Date: April 11, 2008 | By: | /s/ KAREN O. COTTLE<br>Karen O. Cottle<br>Senior Vice President, General Counsel and Secretary |

**EXHIBIT LIST**

| Exhibit Number | Exhibit Description | Incorporated by Reference Form | Date | Number |
|---|---|---|---|---|
| 10.1 | 2003 Equity Incentive Plan, as amended and restated | DEF 14A | 2/27/08 | Appendix A |



ng issues and cost of service studies in upcoming utility rate cases. A hearing was held in April 2016. On October 7, 2016, the Administrative Law Judge issued a recommendation in the docket concerning the value and cost of DG solar installations. On December 20, 2016, the ACC completed its open meeting to consider the recommended opinion and order by the Administrative Law Judge. After making several amendments, the ACC approved the recommended decision by a 4-1 vote. As a result of the ACC's action, effective with APS's 2017 Rate Case Decision, the net metering tariff that governs payments for energy exported to the grid from residential rooftop solar systems was replaced by a more formula-driven approach that utilizes inputs from historical wholesale solar power until an avoided cost methodology is developed by the ACC.

As amended, the decision provides that payments by utilities for energy exported to the grid from DG solar facilities will be determined using a RCP methodology, a method that is based on the most recent five-year rolling average price that APS pays for utility-scale solar projects, while a forecasted avoided cost methodology is being developed. The price established by this RCP method will be updated annually (between general retail rate cases) but will not be decreased by more than 10% per year. Once the avoided cost methodology is developed, the ACC will determine in APS's subsequent rate cases which method (or a combination of methods) is appropriate to determine the actual price to be paid by APS for exported distributed energy.

In addition, the ACC made the following determinations:

- Customers who have interconnected a DG system or submitted an application for interconnection for DG systems prior to September 1, 2017, the date new rates were effective based on APS's 2017 Rate Case Decision, will be grandfathered for a period of 20 years from the date the customer's interconnection application was accepted by the utility;

- Customers with DG solar systems are to be considered a separate class of customers for ratemaking purposes; and

Once an export price is set for APS, no netting or banking of retail credits will be available for new DG customers, and the then-applicable export price will be guaranteed for new customers for a period of 10 years.

This decision of the ACC addresses policy determinations only. The decision states that its principles will be applied in future general retail rate cases, and the policy determinations themselves may be subject to future change, as are all ACC policies. A first-year export energy price of 12.9 cents per kWh is included in the 2017 Settlement Agreement and became effective on September 1, 2017.

In accordance with the 2017 Rate Case Decision, APS filed its request for a second-year export energy price of 11.6 cents per kWh on May 1, 2018. This price reflects the 10% annual reduction discussed above. The new tariff became effective on October 1, 2018.

On January 23, 2017, TASC sought rehearing of the ACC's decision regarding the value and cost of DG. TASC asserted that the ACC improperly ignored the Administrative Procedure Act, failed to give adequate notice regarding the scope of the proceedings, and relied on information that was not submitted as evidence, among other alleged defects. TASC filed a Notice of Appeal in the Arizona Court of Appeals and filed a Complaint and Statutory Appeal in the Maricopa County Superior Court on March 10, 2017. As part of the

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2017 Settlement Agreement described above, TASC agreed to withdraw these appeals when the ACC decision implementing the 2017 Settlement Agreement is no longer subject to appellate review.

**Subpoena from Arizona Corporation Commissioner Robert Burns**

On August 25, 2016, Commissioner Burns, individually and not by action of the ACC as a whole, served subpoenas in APS’s then current retail rate proceeding on APS and Pinnacle West for the production of records and information relating to a range of expenditures from 2011 through 2016. The subpoenas requested information concerning marketing and advertising expenditures, charitable donations, lobbying expenses, contributions to 501(c)(3) and (c)(4) nonprofits and political contributions. The return date for the production of information was set as September 15, 2016. The subpoenas also sought testimony from Company personnel having knowledge of the material, including the Chief Executive Officer.

On September 9, 2016, APS filed with the ACC a motion to quash the subpoenas or, alternatively to stay APS's obligations to comply with the subpoenas and decline to decide APS's motion pending court proceedings. Contemporaneously with the filing of this motion, APS and Pinnacle West filed a complaint for special action and declaratory judgment in the Superior Court of Arizona for Maricopa County, seeking a declaratory judgment that Commissioner Burns’ subpoenas are contrary to law. On September 15, 2016, APS produced all non-confidential and responsive documents and offered to produce any remaining responsive documents that are confidential after an appropriate confidentiality agreement is signed.

On February 7, 2017, Commissioner Burns opened a new ACC docket and indicated that its purpose is to study and rectify problems with transparency and disclosure regarding financial contributions from regulated monopolies or other stakeholders who may appear before the ACC that may directly or indirectly benefit an ACC Commissioner, a candidate for ACC Commissioner, or key ACC Staff. As part of this docket, Commissioner Burns set March 24, 2017 as a deadline for the production of all information previously requested through the subpoenas. Neither APS nor Pinnacle West produced the information requested and instead objected to the subpoena. On March 10, 2017, Commissioner Burns filed suit against APS and Pinnacle West in the Superior Court of Arizona for Maricopa County in an effort to enforce his subpoenas. On March 30, 2017, APS filed a motion to dismiss Commissioner

Burns' suit against APS and Pinnacle West. In response to the motion to dismiss, the court stayed the suit and ordered Commissioner Burns to file a motion to compel the production of the information sought by the subpoenas with the ACC. On June 20, 2017, the ACC denied the motion to compel.

On August 4, 2017, Commissioner Burns amended his complaint to add all of the ACC Commissioners and the ACC itself as defendants. All defendants moved to dismiss the amended complaint. On February 15, 2018, the Superior Court dismissed Commissioner Burns' amended complaint. On March 6, 2018, Commissioner Burns filed an objection to the proposed final order from the Superior Court and a motion to further amend his complaint. The Superior Court permitted Commissioner Burns to amend his complaint to add a claim regarding his attempted investigation into whether his fellow commissioners should have been disqualified from voting on APS's 2017 rate case. Commissioner Burns filed his second amended complaint, and all defendants filed responses opposing the second amended complaint and requested that it be dismissed. Oral argument occurred in November 2018 regarding the motion to dismiss. On December 18, 2018, the trial court granted the defendants' motions to dismiss and entered final judgment on January 18, 2019. On February 13, 2019, Commissioner Burns filed a notice of appeal. APS and Pinnacle West cannot predict the outcome of this matter.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Renewable Energy Ballot Initiative**

On February 20, 2018, a renewable energy advocacy organization filed with the Arizona Secretary of State a ballot initiative for an Arizona constitutional amendment requiring Arizona public service corporations to provide at least 50% of their annual retail sales of electricity from renewable sources by 2030. For purposes of the proposed amendment, eligible renewable sources would not include nuclear generating facilities. The initiative was placed on the November 2018 Arizona elections ballot. On November 6, 2018, the initiative failed to receive adequate voter support and was defeated.

**Energy Modernization Plan**

On January 30, 2018, ACC Commissioner Tobin proposed the Energy Modernization Plan, which consists of a series of energy policies tied to clean energy sources such as energy storage, biomass, energy efficiency, electric vehicles, and expanded energy planning through the IRP process. The Energy Modernization Plan includes replacing the current RES standard with a new standard called the CREST, which incorporates the proposals in the Energy Modernization Plan. On February 22, 2018, the ACC Staff filed a Notice of Inquiry to further examine the matter. As a part of this proposal, the ACC voted in March 2018 to direct utilities to develop a comprehensive biomass generation plan to be included in each utility's RES Implementation Plan. On July 5, 2018, Commissioner Tobin's office issued a set of draft CREST rules for the ACC's consideration.

In August 2018, the ACC directed ACC Staff to open a new rulemaking docket which will address a wide range of energy issues, including the Energy Modernization Plan proposals. The rulemaking will consider possible modifications to existing ACC rules, such as the Renewable Energy Standard, Electric and Gas Energy Efficiency Standards, Net Metering, Resource Planning, and the Biennial Transmission Assessment, as well as the development of new rules regarding forest bioenergy, electric vehicles, interconnection of distributed generation, baseload security, blockchain technology and other technological developments, retail competition, and other energy-related topics. Workshops on these energy issues are scheduled to be held throughout 2019. APS cannot predict the outcome of this matter.

**Integrated Resource Planning**

ACC rules require utilities to develop fifteen-year IRPs which describe how the utility plans to serve customer load in the plan timeframe. The ACC reviews each utility's IRP to determine if it meets the necessary requirements and whether it should be acknowledged. In March of 2018, the ACC reviewed the 2017 IRPs of its jurisdictional utilities and voted to not acknowledge any of the plans. APS does not believe that this lack of acknowledgment will have a material impact on our financial position, results of operations or cash flows. Based on an ACC decision, APS is required to file a Preliminary Resource Plan by April 1, 2019 and its final IRP by April 1, 2020.

**Four Corners**

***SCE-Related Matters***. On December 30, 2013, APS purchased SCE's 48% ownership interest in each of Units 4 and 5 of Four Corners. The 2012 Settlement Agreement includes a procedure to allow APS to request rate adjustments prior to its next general retail rate case related to APS's acquisition of the additional interests in Units 4 and 5 and the related closure of Units 1-3 of Four Corners. APS made its filing under this provision on December 30, 2013. On December 23, 2014, the ACC approved rate adjustments resulting in a revenue increase of $57.1 million on an annual basis. This included the deferral for future recovery of all non-fuel operating costs for the acquired SCE interest in Four Corners, net of the non-fuel operating costs savings

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

resulting from the closure of Units 1-3 from the date of closing of the purchase through its inclusion in rates. The 2012 Settlement Agreement also provided for deferral for future recovery of all unrecovered costs incurred in connection with the closure of Units 1-3. The deferral balance related to the acquisition of SCE’s interest in Units 4 and 5 and the closure of Units 1-3 was $48 million as of December 31, 2018 and is being amortized in rates over a total of 10 years. The ACC's rate adjustment decision was appealed and on September 26, 2017, the Court of Appeals affirmed the ACC's decision on the Four Corners rate adjustment.

As part of APS’s acquisition of SCE’s interest in Units 4 and 5, APS and SCE agreed, via a "Transmission Termination Agreement" that, upon closing of the acquisition, the companies would terminate an existing transmission agreement ("Transmission Agreement") between the parties that provides transmission capacity on a system (the "Arizona Transmission System") for SCE to transmit its portion of the output from Four Corners to California. APS previously submitted a request to FERC related to this termination, which resulted in a FERC order denying rate recovery of $40 million that APS agreed to pay SCE associated with the termination. On December 22, 2015, APS and SCE agreed to terminate the Transmission Termination Agreement and allow for the Transmission Agreement to expire according to its terms, which includes settling obligations in accordance with the terms of the Transmission Agreement. APS established a regulatory asset of $12 million in 2015 in connection with the payment required under the terms of the Transmission Agreement. On July 1, 2016, FERC issued an order denying APS’s request to recover the regulatory asset through its FERC-jurisdictional rates. APS and SCE completed the termination of the Transmission Agreement on July 6, 2016. APS made the required payment to SCE and wrote-off the $12 million regulatory asset and charged operating revenues to reflect the effects of this order in the second quarter of 2016. On July 29, 2016, APS filed a request for rehearing with FERC. In its order denying recovery, FERC also referred to its enforcement division a question of whether the agreement between APS and SCE relating to the settlement of obligations under the Transmission Agreement was a jurisdictional contract that should have been filed with FERC. On October 5, 2017, FERC issued an order denying APS's request for rehearing. FERC also upheld its prior determination that the agreement relating to the settlement was a jurisdictional contract and should have been filed with FERC. APS cannot predict whether or if the enforcement division will take any action. APS filed an appeal of FERC's July 1, 2016 and October 5, 2017 orders with the United States Court of Appeals for the Ninth Circuit on December 4, 2017. That proceeding is pending, and APS cannot predict the outcome of the proceeding.

***SCR Cost Recovery***. On December 29, 2017, in accordance with the 2017 Rate Case Decision, APS filed a Notice of Intent to file its SCR Adjustment to permit recovery of costs associated with the installation of SCR equipment at Four Corners Units 4 and 5. APS filed the SCR Adjustment request in April 2018. Consistent with the 2017 Rate Case Decision, the request was narrow in scope and addressed only costs associated with this specific environmental compliance equipment. The SCR Adjustment request provided that there would be a $67.5 million annual revenue impact that would be applied as a percentage of base rates for all applicable customers. Also, as provided for in the 2017 Rate Case Decision, APS requested that the adjustment become effective no later than January 1, 2019. The hearing for this matter occurred in September 2018. At the hearing, APS accepted ACC Staff's recommendation of a lower annual revenue impact of approximately $58.5 million. The Administrative Law Judge issued a Recommended Opinion and Order finding that the costs for the SCR project were prudently incurred and recommending authorization of the $58.5 million annual revenue requirement related to the installation and operation of the SCRs. Exceptions to the Recommended Opinion and Order were filed by the parties and intervenors on December 7, 2018. The ACC has not issued a decision on this matter. APS anticipates a decision later in 2019.

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### Cholla

On September 11, 2014, APS announced that it would close Unit 2 of Cholla and cease burning coal at the other APS-owned units (Units 1 and 3) at the plant by the mid-2020s, if EPA approves a compromise proposal offered by APS to meet required environmental and emissions standards and rules. On April 14, 2015, the ACC approved APS's plan to retire Unit 2, without expressing any view on the future recoverability of APS's remaining investment in the Unit. APS closed Unit 2 on October 1, 2015. In early 2017, EPA approved a final rule incorporating APS's compromise proposal, which took effect on April 26, 2017.

Previously, APS estimated Cholla Unit 2’s end of life to be 2033. APS has been recovering a return on and of the net book value of the unit in base rates. Pursuant to the 2017 Settlement Agreement described above, APS will be allowed continued recovery of the net book value of the unit and the unit’s decommissioning and other retirement-related costs ($89 million as of December 31, 2018), in addition to a return on its investment. In accordance with GAAP, in the third quarter of 2014, Unit 2’s remaining net book value was reclassified from property, plant and equipment to a regulatory asset. The 2017 Settlement Agreement also shortened the depreciation lives of Cholla Units 1 and 3 to 2026.

**Navajo Plant**

The co-owners of the Navajo Plant and the Navajo Nation agreed that the Navajo Plant will remain in operation until December 2019 under the existing plant lease. The co-owners and the Navajo Nation executed a lease extension on November 29, 2017 that will allow for decommissioning activities to begin after the plant ceases operations in December 2019. Various stakeholders including regulators, tribal representatives, the plant's coal supplier and the U.S. Department of the Interior have been meeting to determine if an alternate solution can be reached that would permit continued operation of the plant beyond 2019. Although we cannot predict whether any alternate plans will be found that would be acceptable to all of the stakeholders and feasible to implement, we believe it is probable that the current owners of the Navajo Plant will cease operations in December 2019.

On February 14, 2017, the ACC opened a docket titled "ACC Investigation Concerning the Future of the Navajo Generating Station" with the stated goal of engaging stakeholders and negotiating a sustainable pathway for the Navajo Plant to continue operating in some form after December 2019. APS cannot predict the outcome of this proceeding.

APS is currently recovering depreciation and a return on the net book value of its interest in the Navajo Plant over its previously estimated life through 2026. APS will seek continued recovery in rates for the book value of its remaining investment in the plant ($88 million as of December 31, 2018) plus a return on the net book value as well as other costs related to retirement and closure, which are still being assessed and may be material. APS believes it will be allowed recovery of the net book value, in addition to a return on its investment. In accordance with GAAP, in the second quarter of 2017, APS's remaining net book value of its interest in the Navajo Plant was reclassified from property, plant and equipment to a regulatory asset. If the ACC does not allow full recovery of the remaining net book value of this interest, all or a portion of the regulatory asset will be written off and APS's net income, cash flows, and financial position will be negatively impacted.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Regulatory Assets and Liabilities

The detail of regulatory assets is as follows (dollars in thousands):

| s | | December 31, 2018 | | December 31, 2017 | |
|---|---|---|---|---|---|
| | Amortization Through | Current | Non-Current | Current | Non-Current |
| Pension | (a) | $— | $733,351 | $— | $576,188 |
| Retired power plant costs | 2033 | 28,182 | 167,164 | 27,402 | 188,843 |
| Income taxes - AFUDC equity | 2048 | 6,457 | 151,467 | 3,828 | 142,852 |
| Deferred fuel and purchased power — mark-to-market (Note 16) | 2023 | 31,728 | 23,768 | 52,100 | 34,845 |
| Deferred fuel and purchased power (b) (c) | 2019 | 37,164 | — | 75,637 | — |
| Four Corners cost deferral | 2024 | 8,077 | 40,228 | 8,077 | 48,305 |
| Income taxes — investment tax credit basis adjustment | 2047 | 1,079 | 25,522 | 1,066 | 26,218 |
| Lost fixed cost recovery (b) | 2019 | 32,435 | — | 59,844 | — |
| Palo Verde VIEs (Note 18) | 2046 | — | 20,015 | — | 19,395 |
| Deferred compensation | 2036 | — | 36,523 | — | 36,413 |
| Deferred property taxes | 2027 | 8,569 | 66,356 | 8,569 | 74,926 |
| Loss on reacquired debt | 2038 | 1,637 | 13,668 | 1,637 | 15,305 |
| Tax expense of Medicare subsidy | 2024 | 1,235 | 6,176 | 1,236 | 7,415 |
| TCA balancing account (b) | 2020 | 3,860 | 772 | 1,220 | — |
| AG-1 deferral | 2022 | 2,654 | 5,819 | 2,654 | 8,472 |
| Mead-Phoenix transmission line CIAC | 2050 | 332 | 10,044 | 332 | 10,376 |
| Coal reclamation | 2026 | 1,546 | 15,607 | 1,068 | 12,396 |
| SCR deferral | N/A | — | 23,276 | — | 353 |
| Other | Various | 1,947 | 3,185 | 3,418 | — |
| Total regulatory assets (d) | | $166,902 | $1,342,941 | $248,088 | $1,202,302 |

(a) This asset represents the future recovery of pension benefit obligations through retail rates. If these costs are disallowed by the ACC, this regulatory asset would be charged to OCI and result in lower future revenues. See Note 7 for further discussion.

(b) See “Cost Recovery Mechanisms” discussion above.

(c) Subject to a carrying charge.

(d) There are no regulatory assets for which the ACC has allowed recovery of costs, but not allowed a return by exclusion from rate base. FERC rates are set using a formula rate as described in “Transmission Rates, Transmission Cost Adjustor and Other Transmission Matters.”

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The detail of regulatory liabilities is as follows (dollars in thousands):

| | Amortization Through | December 31, 2018 | | December 31, 2017 | |
|---|---|---|---|---|---|
| | | Current | Non-Current | Current | Non-Current |
| Excess deferred income taxes - ACC - Tax Cuts and Jobs Act | (a) | $— | $1,272,709 | $— | $1,266,104 |
| Excess deferred income taxes - FERC - Tax Cuts and Jobs Act | 2058 | 6,302 | 243,691 | — | 254,170 |
| Asset retirement obligations | 2057 | — | 278,585 | — | 332,171 |
| Removal costs | (b) | 39,866 | 177,533 | 18,238 | 209,191 |
| Other post retirement benefits | (c) | 37,864 | 125,903 | 37,642 | 151,985 |
| Income taxes - deferred investment tax credit | 2047 | 2,164 | 51,120 | 2,164 | 52,497 |
| Income taxes - change in rates | 2048 | 2,769 | 70,069 | 2,573 | 70,537 |
| Spent nuclear fuel | 2027 | 6,503 | 57,002 | 6,924 | 62,132 |
| Renewable energy standard (d) | 2020 | 44,966 | 20 | 23,155 | — |
| Demand side management (d) | 2020 | 14,604 | 4,123 | 3,066 | 4,921 |
| Sundance maintenance | 2030 | 1,278 | 17,228 | — | 16,897 |
| Deferred gains on utility property | 2022 | 4,423 | 6,581 | 4,423 | 10,988 |
| Four Corners coal reclamation | 2038 | 1,858 | 17,871 | 1,858 | 18,921 |
| Tax expense adjustor mechanism (d) | 2019 | 3,237 | — | — | — |
| Other | Various | 42 | 3,541 | 43 | 2,022 |
| Total regulatory liabilities | | $165,876 | $2,325,976 | $100,086 | $2,452,536 |

(a) While the majority of the excess deferred tax balance shown is subject to special amortization rules under federal income tax laws, which require amortization of the balance over the remaining regulatory life of the related property, treatment of a portion of the liability, and the month in which pass-through of the excess deferred tax balance will begin is subject to regulatory approval. This approval will be sought through the Company's TEAM adjustor mechanism. As a result, the Company cannot estimate the amount of this regulatory liability which is expected to reverse within the next 12 months. See Note 4.

(b) In accordance with regulatory accounting guidance, APS accrues for removal costs for its regulated assets, even if there is no legal obligation for removal.

(c) See Note 7.

(d) See “Cost Recovery Mechanisms” discussion above.

## 4. Income Taxes

Certain assets and liabilities are reported differently for income tax purposes than they are for financial statement purposes. The tax effect of these differences is recorded as deferred taxes. We calculate deferred taxes using currently enacted income tax rates.

APS has recorded regulatory assets and regulatory liabilities related to income taxes on its Balance Sheets in accordance with accounting guidance for regulated operations. The regulatory assets are for certain temporary differences, primarily the allowance for equity funds used during construction, investment tax credit ("ITC") basis adjustment and tax expense of Medicare subsidy. The regulatory liabilities primarily relate to the change in income tax rates and deferred taxes resulting from ITCs.

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On December 22, 2017, the Tax Act was enacted. This legislation made significant changes to the federal income tax laws, including a reduction in the corporate tax rate to 21% effective January 1, 2018. As a result of this rate reduction, the Company recognized a $1.14 billion reduction in its net deferred income tax liabilities as of December 31, 2017.

In accordance with accounting for regulated companies, the effect of this rate reduction is substantially offset by a net regulatory liability. As of December 31, 2017, to reflect the $1.14 billion reduction in its net deferred income tax liabilities caused by the rate reduction, APS has recorded a net regulatory liability of $1.52 billion and a new $377 million net deferred tax asset. The Company will amortize the net regulatory liability in accordance with applicable federal income tax laws, which require the amortization of a majority of the balance over the remaining regulatory life of the related property. As a result of the modifications made to the annual transmission formula rate during the second quarter, the Company has recorded amortization of FERC jurisdictional net excess deferred tax liabilities, retroactive to January 1, 2018. The Company continues to work with the ACC on a plan to amortize the remaining net excess deferred tax liabilities subject to its jurisdiction. See Note 3 for more details.

In August 2018, Treasury proposed regulations that clarify bonus depreciation transition rules under the Tax Act for regulated public utility property placed in service after September 27, 2017 and before January 1, 2018. During the third quarter the Company recorded deferred tax liabilities of approximately $11 million and an increase in its net regulatory liability for excess deferred taxes of approximately $9 million, primarily related to bonus depreciation benefits claimed on the Company’s 2017 tax return as a result of this clarifying guidance. However, the proposed regulations are ambiguous with respect to regulated public utility property placed in service on or after January 1, 2018. On December 20, 2018, the Joint Committee on Taxation (“JCT”) released the general explanation of the Tax Act. The document - commonly referred to as the "Blue Book" - provides a comprehensive technical description of the Tax Act and includes the legislative intent of Congress with respect to the changes made by provisions of the Tax Act. The “Blue Book” provides clarification that the intent of the Tax Act was to exclude from the definition of bonus depreciation qualified property any property placed in service by a regulated public utility after December 31, 2017. In a footnote, the JCT indicated that a technical correction bill may be necessary to reflect this intent.

Management recognizes tax positions which it believes are "more likely than not" to be sustained upon examination. In applying this "more likely than not" assessment, the Company is required to consider the technical merits of a position, including legislative intent. As a result, while no legislation has been passed which clarifies the ambiguities related to bonus depreciation for property placed in service on or after January 1, 2018, the Company currently believes the continued availability of bonus depreciation is not "more likely than not" to be sustained upon examination. As a result, the Company has not recognized any current or deferred tax benefits related to bonus depreciation for property placed in service on or after January 1, 2018.

For the quarter ending March 31, 2018, the Company early adopted ASU 2018-02, Income Statement-Reporting Comprehensive Income: Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income and elected to reclassify the income tax effects of the Tax Act on items within accumulated other comprehensive income to retained earnings. See Note 2 for additional information.

In accordance with regulatory requirements, APS ITCs are deferred and are amortized over the life of the related property with such amortization applied as a credit to reduce current income tax expense in the statement of income.

Net income associated with the Palo Verde sale leaseback VIEs is not subject to tax (see Note 18). As a result, there is no income tax expense associated with the VIEs recorded on the Pinnacle West Consolidated and APS Consolidated Statements of Income.

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a tabular reconciliation of the total amounts of unrecognized tax benefits, excluding interest and penalties, at the beginning and end of the year that are included in accrued taxes and unrecognized tax benefits (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **2016** | **2018** | **2017** | **2016** |
| Total unrecognized tax benefits, January 1 | $41,966 | $36,075 | $34,447 | $41,966 | $36,075 | $34,447 |
| Additions for tax positions of the current year | 3,436 | 2,937 | 2,695 | 3,436 | 2,937 | 2,695 |
| Additions for tax positions of prior years | 2,696 | 4,783 | 886 | 2,696 | 4,783 | 886 |
| Reductions for tax positions of prior years for: | | | | | | |
| Changes in judgment | (1,764 ) | (1,829 ) | (1,953 ) | (1,764 ) | (1,829 ) | (1,953 ) |
| Settlements with taxing authorities | — | — | — | — | — | — |
| Lapses of applicable statute of limitations | (5,603 ) | — | — | (5,603 ) | — | — |
| Total unrecognized tax benefits, December 31 | $40,731 | $41,966 | $36,075 | $40,731 | $41,966 | $36,075 |

Included in the balances of unrecognized tax benefits are the following tax positions that, if recognized, would decrease our effective tax rate (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **2016** | **2018** | **2017** | **2016** |
| Tax positions, that if recognized, would decrease our effective tax rate | $19,504 | $16,373 | $11,313 | $19,504 | $16,373 | $11,313 |

As of the balance sheet date, the tax year ended December 31, 2015 and all subsequent tax years remain subject to examination by the IRS. With a few exceptions, we are no longer subject to state income tax examinations by tax authorities for years before 2014.

We reflect interest and penalties, if any, on unrecognized tax benefits in the Pinnacle West Consolidated and APS Consolidated Statements of Income as income tax expense. The amount of interest expense or benefit recognized related to unrecognized tax benefits are as follows (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **2016** | **2018** | **2017** | **2016** |
| Unrecognized tax benefit interest expense/(benefit) recognized | $(780 ) | $577 | $529 | $(780 ) | $577 | $529 |

Following are the total amount of accrued liabilities for interest recognized related to unrecognized benefits that could reverse and decrease our effective tax rate to the extent matters are settled favorably (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **2016** | **2018** | **2017** | **2016** |
| Unrecognized tax benefit interest accrued | $1,130 | $1,910 | $1,333 | $1,130 | $1,910 | $1,333 |

Additionally, as of December 31, 2018, we have recognized less than $1 million of interest expense to be paid on the underpayment of income taxes for certain adjustments that we have filed, or will file, with the IRS.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The components of income tax expense are as follows (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | Year Ended December 31, | | | Year Ended December 31, | | |
| | 2018 | 2017 | 2016 | 2018 | 2017 | 2016 |
| Current: | | | | | | |
| Federal | $18,375 | $11,624 | $8,630 | $88,180 | $21,512 | $711 |
| State | 3,342 | 3,052 | 1,259 | 1,877 | 2,778 | 4,276 |
| Total current | 21,717 | 14,676 | 9,889 | 90,057 | 24,290 | 4,987 |
| Deferred: | | | | | | |
| Federal | 94,721 | 223,729 | 201,743 | 32,436 | 221,078 | 215,178 |
| State | 17,464 | 19,867 | 24,779 | 22,321 | 23,800 | 25,677 |
| Total deferred | 112,185 | 243,596 | 226,522 | 54,757 | 244,878 | 240,855 |
| Income tax expense | $133,902 | $258,272 | $236,411 | $144,814 | $269,168 | $245,842 |

The following chart compares pretax income at the statutory federal income tax rate of 21% in 2018 and 35% in 2017 and 2016 to income tax expense (dollars in thousands):

| | Pinnacle West Consolidated | | | APS Consolidated | | |
|---|---|---|---|---|---|---|
| | Year Ended December 31, | | | Year Ended December 31, | | |
| | 2018 | 2017 | 2016 | 2018 | 2017 | 2016 |
| Federal income tax expense at statutory rate | $139,533 | $268,177 | $244,278 | $154,260 | $277,540 | $254,617 |
| Increases (reductions) in tax expense resulting from: | | | | | | |
| State income tax net of federal income tax benefit | 16,411 | 14,897 | 16,311 | 19,091 | 17,276 | 18,750 |
| Nondeductible expenditures associated with ballot initiative | 7,879 | — | — | — | — | — |
| Stock compensation | (1,804) | (6,659) | (2,951) | (780) | (3,489) | (1,937) |
| Excess deferred income taxes - Tax Cuts and Jobs Act | (6,725) | 9,348 | — | (4,715) | 9,431 | — |
| Allowance for equity funds used during construction (see Note 1) | (7,231) | (12,937) | (11,724) | (7,231) | (12,937) | (11,724) |
| Palo Verde VIE noncontrolling interest (see Note 18) | (4,094) | (6,823) | (6,823) | (4,094) | (6,823) | (6,823) |
| Investment tax credit amortization | (6,742) | (6,715) | (5,887) | (6,742) | (6,715) | (5,887) |
| Other | (3,325) | (1,016) | 3,207 | (4,975) | (5,115) | (1,154) |
| Income tax expense | $133,902 | $258,272 | $236,411 | $144,814 | $269,168 | $245,842 |

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The components of the net deferred income tax liability were as follows (dollars in thousands):

| | Pinnacle West Consolidated | | APS Consolidated | |
|---|---|---|---|---|
| | December 31, | | December 31, | |
| | 2018 | 2017 | 2018 | 2017 |
| DEFERRED TAX ASSETS | | | | |
| Risk management activities | $15,785 | $25,103 | $15,785 | $25,103 |
| Regulatory liabilities: | | | | |
| Excess deferred income taxes - Tax Cuts and Jobs Act | 376,869 | 376,906 | 376,869 | 376,906 |
| Asset retirement obligation and removal costs | 117,201 | 135,847 | 117,201 | 135,847 |
| Unamortized investment tax credits | 53,284 | 54,661 | 53,284 | 54,661 |
| Other postretirement benefits | 40,532 | 47,021 | 40,532 | 47,021 |
| Other | 40,380 | 37,489 | 40,380 | 37,489 |
| Pension liabilities | 112,019 | 83,126 | 107,009 | 77,280 |
| Coal reclamation liabilities | 47,508 | 45,802 | 47,508 | 45,802 |
| Renewable energy incentives | 30,779 | 33,546 | 30,779 | 33,546 |
| Credit and loss carryforwards | 1,755 | 53,946 | — | 1,920 |
| Other | 58,820 | 56,630 | 59,919 | 62,421 |
| Total deferred tax assets | 894,932 | 950,077 | 889,266 | 897,996 |
| DEFERRED TAX LIABILITIES | | | | |
| Plant-related | (2,277,724) | (2,220,886) | (2,277,724) | (2,220,886) |
| Risk management activities | (237) | (491) | (237) | (491) |
| Other postretirement assets and other special use funds | (57,697) | (66,134) | (57,274) | (65,733) |
| Regulatory assets: | | | | |
| Allowance for equity funds used during construction | (39,086) | (36,365) | (39,086) | (36,365) |
| Deferred fuel and purchased power | (23,086) | (40,778) | (23,086) | (40,778) |
| Pension benefits | (181,504) | (142,848) | (181,504) | (142,848) |
| Retired power plant costs (see Note 3) | (48,348) | (53,611) | (48,348) | (53,611) |
| Other | (72,096) | (74,423) | (72,096) | (74,423) |
| Other | (2,575) | (5,346) | (2,575) | (5,346) |
| Total deferred tax liabilities | (2,702,353) | (2,640,882) | (2,701,930) | (2,640,481) |
| Deferred income taxes — net | $(1,807,421) | $(1,690,805) | $(1,812,664) | $(1,742,485) |

As of December 31, 2018, the deferred tax assets for credit and loss carryforwards relate primarily to federal general business credits of approximately $14 million, which first begin to expire in 2036, and state credit carryforwards net of federal benefit of $7 million, which first begin to expire in 2023. The credit and loss carryforwards amount above has been reduced by $19 million of unrecognized tax benefits.

## 5. Lines of Credit and Short-Term Borrowings

Pinnacle West and APS maintain committed revolving credit facilities in order to enhance liquidity and provide credit support for their commercial paper programs, to refinance indebtedness, and for other general corporate purposes.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The table below presents the consolidated credit facilities and the amounts available and outstanding as of December 31, 2018 and 2017 (dollars in thousands):

| | December 31, 2018 | | | December 31, 2017 | | |
|---|---|---|---|---|---|---|
| | Pinnacle West | APS | Total | Pinnacle West | APS | Total |
| Commitments under Credit Facilities | $350,000 | $1,000,000 | $1,350,000 | $325,000 | $1,000,000 | $1,325,000 |
| Outstanding Commercial Paper and Revolving Credit Facility Borrowings | (76,400) | — | (76,400) | (95,400) | — | (95,400) |
| Amount of Credit Facilities Available | $273,600 | $1,000,000 | $1,273,600 | $229,600 | $1,000,000 | $1,229,600 |
| Weighted-Average Commitment Fees | 0.125% | 0.100% | | 0.125% | 0.100% | |

### *Pinnacle West*

On June 28, 2018, Pinnacle West refinanced its 364-day $125 million unsecured revolving credit facility that would have matured on July 30, 2018 with a new 364-day $150 million credit facility that matures June 27, 2019. Borrowings under the facility bear interest at LIBOR plus 0.70% per annum. At December 31, 2018, Pinnacle West had $54 million outstanding under the facility.

On July 12, 2018, Pinnacle West replaced its $200 million revolving credit facility that would have matured in May 2021, with a new $200 million facility that matures in July 2023. Pinnacle West has the option to increase the amount of the facility up to a maximum of $300 million upon the satisfaction of certain conditions and with the consent of the lenders. At December 31, 2018, Pinnacle West had no outstanding borrowings under its credit facility, no letters of credit outstanding and $22 million of commercial paper borrowings.

### *APS*

On July 12, 2018, APS replaced its $500 million revolving credit facility that would have matured in May 2021, with a new $500 million facility that matures in July 2023.

At December 31, 2018, APS had two revolving credit facilities totaling $1 billion, including a $500 million credit facility that matures in June 2022 and the above-mentioned $500 million facility. APS may increase the amount of each facility up to a maximum of $700 million, for a total of $1.4 billion, upon the satisfaction of certain conditions and with the consent of the lenders. Interest rates are based on APS’s senior unsecured debt credit ratings. These facilities are available to support APS’s $500 million commercial paper program, for bank borrowings or for issuances of letters of credit. At December 31, 2018, APS had no commercial paper outstanding and no outstanding borrowings or letters of credit under its revolving credit facilities. See "Financial Assurances" in Note 10 for a discussion of APS's other outstanding letters of credit.

**Debt Provisions**

On November 27, 2018, the ACC issued a financing order in which, subject to specified parameters and procedures, it approved APS’s short-term debt authorization equal to a sum of (i) 7% of APS’s capitalization, and (ii) $500 million (which is required to be used for costs relating to purchases of natural gas and power). See Note 6 for additional long-term debt provisions.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 6. Long-Term Debt and Liquidity Matters

All of Pinnacle West's and APS's debt is unsecured. The following table presents the components of long-term debt on the Consolidated Balance Sheets outstanding at December 31, 2018 and 2017 (dollars in thousands):

| | Maturity Dates (a) | Interest Rates | December 31, 2018 | 2017 |
|---|---|---|---|---|
| **APS** | | | | |
| Pollution control bonds: | | | | |
| Variable | 2029 | (b) | $35,975 | $35,975 |
| Fixed | 2024 | 4.70% | 115,150 | 147,150 |
| Total pollution control bonds | | | 151,125 | 183,125 |
| Senior unsecured notes | 2019-2048 | 2.20%-8.75% | 4,575,000 | 4,275,000 |
| Term loans | | (c) | — | 150,000 |
| Unamortized discount | | | (12,638) | (11,288) |
| Unamortized premium | | | 7,736 | 8,049 |
| Unamortized debt issuance cost | | | (31,787) | (31,594) |
| Total APS long-term debt | | | 4,689,436 | 4,573,292 |
| Less current maturities | | | 500,000 | 82,000 |
| Total APS long-term debt less current maturities | | | 4,189,436 | 4,491,292 |
| **Pinnacle West** | | | | |
| Senior unsecured notes | 2020 | 2.25% | 300,000 | 300,000 |
| Term loan | 2020 | (d) | 150,000 | — |
| Unamortized discount | | | (121) | (184) |
| Unamortized debt issuance cost | | | (1,083) | (1,395) |
| Total Pinnacle West long-term debt | | | 448,796 | 298,421 |
| Less current maturities | | | — | — |
| Total Pinnacle West long-term debt less current maturities | | | 448,796 | 298,421 |
| **TOTAL LONG-TERM DEBT LESS CURRENT MATURITIES** | | | $4,638,232 | $4,789,713 |

(a) This schedule does not reflect the timing of redemptions that may occur prior to maturities.

(b) The weighted-average rate for the variable rate pollution control bonds was 1.76% at December 31, 2018 and 1.77% at December 31, 2017.

(c) The weighted-average interest rate was 2.24% at December 31, 2017.

(d) The weighted-average interest rate was 3.02% at December 31, 2018.

The following table shows principal payments due on Pinnacle West's and APS's total long-term debt (dollars in thousands):

| Year | Consolidated Pinnacle West | Consolidated APS |
|---|---|---|
| 2019 | $500,000 | $500,000 |

| | | |
|---|---|---|
| 2020 | 700,000 | 250,000 |
| 2021 | — | — |
| 2022 | — | — |
| 2023 | — | — |
| Thereafter | 3,976,125 | 3,976,125 |
| Total | $5,176,125 | $4,726,125 |

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## Debt Fair Value

Our long-term debt fair value estimates are classified within Level 2 of the fair value hierarchy. The following table represents the estimated fair value of our long-term debt, including current maturities (dollars in thousands):

| | As of December 31, 2018 | | As of December 31, 2017 | |
|---|---|---|---|---|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Pinnacle West | $448,796 | $443,955 | $298,421 | $298,608 |
| APS | 4,689,436 | 4,789,608 | 4,573,292 | 5,006,348 |
| Total | $5,138,232 | $5,233,563 | $4,871,713 | $5,304,956 |

## Credit Facilities and Debt Issuances

### *Pinnacle West*

On December 21, 2018, Pinnacle West entered into a $150 million term loan facility that matures December 2020. The proceeds were used for general corporate purposes.

### *APS*

On May 30, 2018, APS purchased all $32 million of Maricopa County, Arizona Pollution Control Corporation Pollution Control Revenue Refunding Bonds, 2009 Series C, due 2029. These bonds were classified as current maturities of long-term debt on our Consolidated Balance Sheets at December 31, 2017.

On June 26, 2018, APS repaid at maturity APS's $50 million term loan facility.

On August 9, 2018, APS issued $300 million of 4.20% unsecured senior notes that mature on August 15, 2048. The net proceeds from the sale of the notes were used to repay commercial paper borrowings.

On November 30, 2018, APS repaid its $100 million term loan facility that would have matured April 22, 2019.

On December 21, 2018, Pinnacle West contributed $150 million into APS in the form of an equity infusion. APS used this contribution to repay short-term indebtedness.

See “Lines of Credit and Short-Term Borrowings” in Note 5 and “Financial Assurances” in Note 10 for discussion of APS’s separate outstanding letters of credit.

**Debt Provisions**

Pinnacle West’s and APS’s debt covenants related to their respective bank financing arrangements include maximum debt to capitalization ratios. Pinnacle West and APS comply with this covenant.  For both Pinnacle West and APS, this covenant requires that the ratio of consolidated debt to total consolidated capitalization not exceed 65%.  At December 31, 2018, the ratio was approximately 50% for Pinnacle West and 46% for APS.  Failure to comply with such covenant levels would result in an event of default, which, generally speaking, would require the immediate repayment of the debt subject to the covenants and could cross-default other debt.  See further discussion of “cross-default” provisions below.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Neither Pinnacle West's nor APS's financing agreements contain "rating triggers" that would result in an acceleration of the required interest and principal payments in the event of a rating downgrade. However, our bank credit agreements contain a pricing grid in which the interest rates we pay for borrowings thereunder are determined by our current credit ratings.

All of Pinnacle West's loan agreements contain "cross-default" provisions that would result in defaults and the potential acceleration of payment under these loan agreements if Pinnacle West or APS were to default under certain other material agreements. All of APS's bank agreements contain "cross-default" provisions that would result in defaults and the potential acceleration of payment under these bank agreements if APS were to default under certain other material agreements. Pinnacle West and APS do not have a material adverse change restriction for credit facility borrowings.

Although provisions in APS's articles of incorporation and ACC financing orders establish maximum amounts of preferred stock and debt that APS may issue, APS does not expect any of these provisions to limit its ability to meet its capital requirements. On November 27, 2018, the ACC issued a financing order in which, subject to specified parameters and procedures, it approved an increase in APS's long-term debt authorization from$5.1 billion to $5.9 billion in light of the projected growth of APS and its customer base and the resulting projected financing needs. See Note 5 for additional short-term debt provisions.

### 7. Retirement Plans and Other Postretirement Benefits

Pinnacle West sponsors a qualified defined benefit and account balance pension plan (The Pinnacle West Capital Corporation Retirement Plan) and a non-qualified supplemental excess benefit retirement plan for the employees of Pinnacle West and its subsidiaries. All new employees participate in the account balance plan. Defined benefit plans specify the amount of benefits a plan participant is to receive using information about the participant. The pension plan covers nearly all employees. The supplemental excess benefit retirement plan covers officers of the Company and highly compensated employees designated for participation by the Board of Directors. Our employees do not contribute to the plans. We calculate the benefits based on age, years of service and pay.

Pinnacle West also sponsors other postretirement benefit plans (Pinnacle West Capital Corporation Group Life and Medical Plan and Pinnacle West Capital Corporation Post-65

Retiree Health Reimbursement Arrangement) for the employees of Pinnacle West and its subsidiaries. These plans provide medical and life insurance benefits to retired employees. Employees must retire to become eligible for these retirement benefits, which are based on years of service and age. For the medical insurance plan, retirees make contributions to cover a portion of the plan costs. For the life insurance plan, retirees do not make contributions. We retain the right to change or eliminate these benefits.

Because of plan changes in 2014, the Company sought IRS approval to move approximately $186 million of other postretirement benefit trust assets into a new trust account to pay for active union employee medical costs. In December 2016, FERC approved a methodology for determining the amount of other postretirement benefit trust assets to transfer into a new trust account to pay for active union employee medical costs. On January 2, 2018, these funds were moved to the new trust account, which is included in the other special use funds on the Consolidated Balance Sheets. The Company and the IRS executed a final Closing Agreement on March 2, 2018. The Company made an informational filing with FERC during February 2018. It is the Company’s understanding that completion of these regulatory requirements permits access to approximately $186 million for the sole purpose of paying active union employee medical benefits.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Pinnacle West uses a December 31 measurement date each year for its pension and other postretirement benefit plans. The market-related value of our plan assets is their fair value at the measurement date. See Note 13 for further discussion of how fair values are determined. Due to subjective and complex judgments, which may be required in determining fair values, actual results could differ from the results estimated through the application of these methods.

A significant portion of the changes in the actuarial gains and losses of our pension and postretirement plans is attributable to APS and therefore is recoverable in rates. Accordingly, these changes are recorded as a regulatory asset or regulatory liability.

The following table provides details of the plans' net periodic benefit costs and the portion of these costs charged to expense (including administrative costs and excluding amounts capitalized as overhead construction or billed to electric plant participants) (dollars in thousands):

| | **Pension** | | | **Other Benefits** | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **2016** | **2018** | **2017** | **2016** |
| Service cost-benefits earned during the period | $56,669 | $54,858 | $53,792 | $21,100 | $17,119 | $14,993 |
| Interest cost on benefit obligation | 124,689 | 129,756 | 131,647 | 28,147 | 29,959 | 29,721 |
| Expected return on plan assets | (182,853) | (174,271) | (173,906) | (42,082) | (53,401) | (36,495) |
| Amortization of: | | | | | | |
| Prior service cost (credit) | — | 81 | 527 | (37,842) | (37,842) | (37,883) |
| Net actuarial loss | 32,082 | 47,900 | 40,717 | — | 5,118 | 4,589 |
| Net periodic benefit cost (benefit) | $30,587 | $58,324 | $52,777 | $(30,677) | $(39,047) | $(25,075) |
| Portion of cost charged to expense | $10,120 | $27,295 | $26,172 | $(21,426) | $(18,274) | $(12,435) |

On January 1, 2018, we adopted new accounting standard ASU 2017-07, Compensation-Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. This new standard changed our income statement presentation of net periodic benefit cost/(credits) and allows only the service cost component of net periodic benefit cost to be eligible for capitalization. See Note 2 for additional information.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table shows the plans' changes in the benefit obligations and funded status for the years 2018 and 2017 (dollars in thousands):

| | Pension | | Other Benefits | |
|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 |
| **Change in Benefit Obligation** | | | | |
| Benefit obligation at January 1 | $3,394,186 | $3,204,462 | $753,393 | $716,445 |
| Service cost | 56,669 | 54,858 | 21,100 | 17,119 |
| Interest cost | 124,689 | 129,756 | 28,147 | 29,959 |
| Benefit payments | (184,161) | (166,342) | (31,540) | (30,144) |
| Actuarial (gain) loss | (200,757) | 171,452 | (94,329) | 20,014 |
| Benefit obligation at December 31 | 3,190,626 | 3,394,186 | 676,771 | 753,393 |
| **Change in Plan Assets** | | | | |
| Fair value of plan assets at January 1 | 3,057,027 | 2,675,357 | 1,022,371 | 882,651 |
| Actual return on plan assets | (201,078) | 428,374 | (40,354) | 139,367 |
| Employer contributions | 50,000 | 100,000 | — | 353 |
| Benefit payments | (172,473) | (146,704) | (72,453) | — |
| Transfer to active union medical account | — | — | (185,887) | — |
| Fair value of plan assets at December 31 | 2,733,476 | 3,057,027 | 723,677 | 1,022,371 |
| **Funded Status at December 31** | $(457,150) | $(337,159) | $46,906 | $268,978 |

The following table shows the projected benefit obligation and the accumulated benefit obligation for pension plans with an accumulated obligation in excess of plan assets as of December 31, 2018 and 2017 (dollars in thousands):

| | 2018 | 2017 |
|---|---|---|
| Projected benefit obligation | $3,190,626 | $3,394,186 |
| Accumulated benefit obligation | 3,038,774 | 3,227,233 |
| Fair value of plan assets | 2,733,476 | 3,057,027 |

The following table shows the amounts recognized on the Consolidated Balance Sheets as of December 31, 2018 and 2017 (dollars in thousands):

| | Pension | | Other Benefits | |
|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 |
| Noncurrent asset | $— | $— | $46,906 | $268,978 |
| Current liability | (13,980) | (9,859) | — | — |
| Noncurrent liability | (443,170) | (327,300) | — | — |
| Net amount recognized | $(457,150) | $(337,159) | $46,906 | $268,978 |

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table shows the details related to accumulated other comprehensive loss as of December 31, 2018 and 2017 (dollars in thousands):

| | Pension | | Other Benefits | |
|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 |
| Net actuarial loss | $794,292 | $643,199 | $63,544 | $75,439 |
| Prior service credit | — | — | (227,733) | (265,575) |
| APS's portion recorded as a regulatory (asset) liability | (733,351 ) | (576,188 ) | 163,767 | 189,627 |
| Income tax expense (benefit) | (15,083 ) | (24,915 ) | 561 | 853 |
| Accumulated other comprehensive loss | $45,858 | $42,096 | $139 | $344 |

The following table shows the estimated amounts that will be amortized from accumulated other comprehensive loss and regulatory assets and liabilities into net periodic benefit cost in 2019 (dollars in thousands):

| | Pension | Other Benefits |
|---|---|---|
| Net actuarial loss | $43,248 | $— |
| Prior service credit | — | (37,821 ) |
| Total amounts estimated to be amortized from accumulated other comprehensive loss (gain) and regulatory assets (liabilities) in 2019 | $43,248 | $(37,821 ) |

The following table shows the weighted-average assumptions used for both the pension and other benefits to determine benefit obligations and net periodic benefit costs:

| | Benefit Obligations As of December 31, | | Benefit Costs For the Years Ended December 31, | | |
|---|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 | 2016 |
| Discount rate – pension | 4.34 % | 3.65 % | 3.65 % | 4.08 % | 4.37 % |
| Discount rate – other benefits | 4.39 % | 3.71 % | 3.71 % | 4.17 % | 4.52 % |
| Rate of compensation increase | 4.00 % | 4.00 % | 4.00 % | 4.00 % | 4.00 % |
| Expected long-term return on plan assets - pension | N/A | N/A | 6.05 % | 6.55 % | 6.90 % |
| Expected long-term return on plan assets - other benefits | N/A | N/A | 5.40 % | 6.05 % | 4.45 % |
| Initial healthcare cost trend rate (pre-65 participants) | 7.00 % | 7.00 % | 7.00 % | 7.00 % | 7.00 % |
| Initial healthcare cost trend rate (post-65 participants) | 4.75 % | 4.75 % | 4.75 % | 5.00 % | 5.00 % |
| Ultimate healthcare cost trend rate | 4.75 % | 4.75 % | 4.75 % | 5.00 % | 5.00 % |
| Number of years to ultimate trend rate (pre-65 participants) | 7 | 8 | 8 | 4 | 4 |

In selecting the pretax expected long-term rate of return on plan assets, we consider past performance and economic forecasts for the types of investments held by the plan. For 2019, we are assuming a 6.25% long-term rate of return for pension assets and 5.55% (before tax) for other benefit assets, which we believe is reasonable given our asset allocation in relation to historical and expected performance.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In selecting our healthcare trend rates, we consider past performance and forecasts of healthcare costs. A one percentage point change in the assumed initial and ultimate healthcare cost trend rates would have the following effects on our December 31, 2018 amounts (dollars in thousands):

| | 1% Increase | 1% Decrease |
|---|---|---|
| Effect on other postretirement benefits expense, after consideration of amounts capitalized or billed to electric plant participants | $ 10,235 | $ (4,322 ) |
| Effect on service and interest cost components of net periodic other postretirement benefit costs | 11,223 | (8,479 ) |
| Effect on the accumulated other postretirement benefit obligation | 101,224 | (81,144 ) |

### Plan Assets

The Board of Directors has delegated oversight of the pension and other postretirement benefit plans' assets to an Investment Management Committee ("Committee"). The Committee has adopted investment policy statements ("IPS") for the pension and the other postretirement benefit plans' assets. The investment strategies for these plans include external management of plan assets, and prohibition of investments in Pinnacle West securities.

The overall strategy of the pension plan's IPS is to achieve an adequate level of trust assets relative to the benefit obligations. To achieve this objective, the plan's investment policy provides for mixes of investments including long-term fixed income assets and return-generating assets. The target allocation between return-generating and long-term fixed income assets is defined in the IPS and is a function of the plan's funded status. The plan's funded status is reviewed on at least a monthly basis.

Changes in the value of long-term fixed income assets, also known as liability-hedging assets, are intended to offset changes in the benefit obligations due to changes in interest rates. Long-term fixed income assets consist primarily of fixed income debt securities issued by the U.S. Treasury and other government agencies, U.S. Treasury Futures Contracts, and fixed income debt securities issued by corporations. Long-term fixed income assets may also include interest rate swaps, and other instruments.

Return-generating assets are intended to provide a reasonable long-term rate of investment return with a prudent level of volatility. Return-generating assets are composed of U.S. equities, international equities, and alternative investments. International equities include investments in both developed and emerging markets. Alternative investments include investments in real estate, private equity and various other strategies. The plan may also hold investments in return-generating assets by holding securities in partnerships, common and collective trusts and mutual funds.

Based on the IPS, and given the pension plan's funded status at year-end 2018, the target and actual allocation for the pension plan at December 31, 2018 are as follows:

| | Pension | |
|---|---|---|
| | **Target Allocation** | **Actual Allocation** |
| Long-term fixed income assets | 62 % | 64 % |
| Return-generating assets | 38 % | 36 % |
| Total | 100 % | 100 % |

The permissible range is within +/- 3% of the target allocation shown in the above table, and also considers the Plan's funded status.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the additional target allocations, as a percent of total pension plan assets, for the return-generating assets:

| Asset Class | Target Allocation | |
|---|---|---|
| Equities in US and other developed markets | 18 | % |
| Equities in emerging markets | 6 | % |
| Alternative investments | 14 | % |
| Total | 38 | % |

The pension plan IPS does not provide for a specific mix of long-term fixed income assets, but does expect the average credit quality of such assets to be investment grade.

As of December 31, 2018, the asset allocation for other postretirement benefit plan assets is governed by the IPS for those plans, which provides for different asset allocation target mixes depending on the characteristics of the liability. Some of these asset allocation target mixes vary with the plan's funded status. The following table presents the actual allocations of the investment for the other postretirement benefit plan at December 31, 2018:

| | Other Benefits Actual Allocation | |
|---|---|---|
| Long-term fixed income assets | 69 | % |
| Return-generating assets | 31 | % |
| Total | 100 | % |

See Note 13 for a discussion on the fair value hierarchy and how fair value methodologies are applied. The plans invest directly in fixed income, U.S. Treasury Futures Contracts, and equity securities, in addition to investing indirectly in fixed income securities, equity securities and real estate through the use of mutual funds, partnerships and common and collective trusts. Equity securities held directly by the plans are valued using quoted active market prices from the published exchange on which the equity security trades, and are classified as Level 1. U.S. Treasury Futures Contracts are valued using the quoted active market prices from the exchange on which they trade, and are classified as Level 1. Fixed income securities issued by the U.S. Treasury held directly by the plans are valued using quoted active market prices, and are classified as Level 1. Fixed income securities issued by corporations, municipalities, and other agencies are primarily valued using quoted inactive market prices, or quoted active market prices for similar securities, or by utilizing calculations which incorporate observable inputs such as yield, maturity and credit quality. These instruments are classified as Level 2.

Mutual funds, partnerships, and common and collective trusts are valued utilizing a net asset value (NAV) concept or its equivalent. Mutual funds, which includes exchange traded funds (ETFs), are classified as Level 1 and valued using a NAV that is observable and based on the active market in which the fund trades.

Common and collective trusts are maintained by banks or investment companies and hold certain investments in accordance with a stated set of objectives (such as tracking the performance of the S&P 500 Index). The trust's shares are offered to a limited group of investors, and are not traded in an active market. Investments in common and collective trusts are valued using NAV as a practical expedient and, accordingly, are not classified in the fair value hierarchy. The NAV for trusts investing in exchange traded equities, and fixed income securities is derived from the market prices of the underlying securities held by the trusts. The

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NAV for trusts investing in real estate is derived from the appraised values of the trust's underlying real estate assets. As of December 31, 2018, the plans were able to transact in the common and collective trusts at NAV.

Investments in partnerships are also valued using the concept of NAV as a practical expedient and, accordingly, are not classified in the fair value hierarchy. The NAV for these investments is derived from the value of the partnerships' underlying assets. The plan's partnerships holdings relate to investments in high-yield fixed income instruments and assets of privately held portfolio companies. Certain partnerships also include funding commitments that may require the plan to contribute up to $75 million to these partnerships; as of December 31, 2018, approximately $62 million of these commitments have been funded.

The plans’ trustee provides valuation of our plan assets by using pricing services that utilize methodologies described to determine fair market value. We have internal control procedures to ensure this information is consistent with fair value accounting guidance. These procedures include assessing valuations using an independent pricing source, verifying that pricing can be supported by actual recent market transactions, assessing hierarchy classifications, comparing investment returns with benchmarks, and obtaining and reviewing independent audit reports on the trustee’s internal operating controls and valuation processes.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The fair value of Pinnacle West's pension plan and other postretirement benefit plan assets at December 31, 2018, by asset category, are as follows (dollars in thousands):

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Other (a) | Balance at December 31, 2018 |
|---|---|---|---|---|
| **Pension Plan:** | | | | |
| Cash and cash equivalents | $ 451 | $— | $— | $ 451 |
| Fixed income securities: | | | | |
| Corporate | — | 1,237,744 | — | 1,237,744 |
| U.S. Treasury | 372,649 | — | — | 372,649 |
| Other (b) | — | 78,902 | — | 78,902 |
| Common stock equities (c) | 196,661 | — | — | 196,661 |
| Mutual funds (d) | 120,976 | — | — | 120,976 |
| Common and collective trusts: | | | | |
| Equities | — | — | 272,926 | 272,926 |
| Real estate | — | — | 165,123 | 165,123 |
| Fixed Income | — | — | 86,483 | 86,483 |
| Partnerships | — | — | 125,217 | 125,217 |
| Short-term investments and other (e) | — | — | 76,344 | 76,344 |
| Total | $ 690,737 | $ 1,316,646 | $ 726,093 | $ 2,733,476 |
| **Other Benefits:** | | | | |
| Cash and cash equivalents | $ 93 | $— | $— | $ 93 |
| Fixed income securities: | | | | |
| Corporate | — | 163,286 | — | 163,286 |
| U.S. Treasury | 318,017 | — | — | 318,017 |
| Other (b) | — | 7,531 | — | 7,531 |
| Common stock equities (c) | 129,199 | — | — | 129,199 |
| Mutual funds (d) | 10,963 | — | — | 10,963 |
| Common and collective trusts: | | | | |
| Equities | — | — | 65,720 | 65,720 |
| Real estate | — | — | 19,054 | 19,054 |
| Short-term investments and other (e) | 3,633 | — | 6,181 | 9,814 |
| Total | $ 461,905 | $ 170,817 | $ 90,955 | $ 723,677 |

(a) These investments primarily represent assets valued using net asset value as a practical expedient, and have not been classified in the fair value hierarchy.
(b) This category consists primarily of debt securities issued by municipalities.
(c) This category primarily consists of U.S. common stock equities.
(d) These funds invest in international common stock equities.
(e) This category includes plan receivables and payables.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The fair value of Pinnacle West's pension plan and other postretirement benefit plan assets at December 31, 2017, by asset category, are as follows (dollars in thousands):

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Other (a) | Balance at December 31, 2017 |
|---|---|---|---|---|
| **Pension Plan:** | | | | |
| Cash and cash equivalents | $ 3,830 | $— | $— | $ 3,830 |
| Fixed income securities: | | | | |
| Corporate | — | 1,365,194 | — | 1,365,194 |
| U.S. Treasury | 221,291 | — | — | 221,291 |
| Other (b) | — | 100,599 | — | 100,599 |
| Common stock equities (c) | 228,088 | — | — | 228,088 |
| Mutual funds (d) | 233,732 | — | — | 233,732 |
| Common and collective trusts: | | | | |
| Equities | — | — | 408,763 | 408,763 |
| Real estate | — | — | 171,569 | 171,569 |
| Fixed Income | — | — | 90,869 | 90,869 |
| Partnerships | — | — | 133,379 | 133,379 |
| Short-term investments and other (e) | — | 1,208 | 98,505 | 99,713 |
| Total | $ 686,941 | $ 1,467,001 | $ 903,085 | $ 3,057,027 |
| **Other Benefits:** | | | | |
| Cash and cash equivalents | $ 143 | $— | $— | $ 143 |
| Fixed income securities: | | | | |
| Corporate | — | 306,008 | — | 306,008 |
| U.S. Treasury | 336,963 | — | — | 336,963 |
| Other (b) | — | 32,508 | — | 32,508 |
| Common stock equities (c) | 196,153 | — | — | 196,153 |
| Mutual funds (d) | 39,269 | — | — | 39,269 |
| Common and collective trusts: | | | | |
| Equities | — | — | 75,310 | 75,310 |
| Real estate | — | — | 15,422 | 15,422 |
| Short-term investments and other (e) | 11,268 | 149 | 9,178 | 20,595 |
| Total | $ 583,796 | $ 338,665 | $ 99,910 | $ 1,022,371 |

(a) These investments primarily represent assets valued using net asset value as a practical expedient, and have not been classified in the fair value hierarchy.
(b) This category consists primarily of debt securities issued by municipalities.
(c) This category primarily consists of U.S. common stock equities.
(d) These funds invest in U.S. and international common stock equities.
(e) This category includes plan receivables and payables.

**Contributions**

Future year contribution amounts are dependent on plan asset performance and plan actuarial assumptions. We made contributions to our pension plan totaling $50 million in 2018, $100 million in 2017, and $100 million in 2016. The minimum required contributions for the pension plan are zero for the next three years. We expect to make voluntary contributions up to a total of $350 million during the 2019-2021 period.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

With regard to contributions to our other postretirement benefit plan, we did not make a contribution in 2018. We made a contribution of approximately $1 million in each of 2017 and 2016. We do not expect to make any contributions over the next three years to our other postretirement benefit plans. In 2018, the Company was reimbursed $72 million for prior years retiree medical claims from the other postretirement benefit plan trust assets.

### Estimated Future Benefit Payments

Benefit payments, which reflect estimated future employee service, for the next five years and the succeeding five years thereafter, are estimated to be as follows (dollars in thousands):

| Year | Pension | Other Benefits |
|---|---|---|
| 2019 | $ 188,492 | $ 32,622 |
| 2020 | 193,087 | 34,199 |
| 2021 | 198,471 | 35,551 |
| 2022 | 204,399 | 36,673 |
| 2023 | 211,346 | 37,405 |
| Years 2024-2028 | 1,093,319 | 187,023 |

Electric plant participants contribute to the above amounts in accordance with their respective participation agreements.

### Employee Savings Plan Benefits

Pinnacle West sponsors a defined contribution savings plan for eligible employees of Pinnacle West and its subsidiaries. In 2018, costs related to APS's employees represented 99% of the total cost of this plan. In a defined contribution savings plan, the benefits a participant receives result from regular contributions participants make to their own individual account, the Company's matching contributions and earnings or losses on their investments. Under this plan, the Company matches a percentage of the participants' contributions in cash which is then invested in the same investment mix as participants elect to invest their own future contributions. Pinnacle West recorded expenses for this plan of approximately $11 million for 2018, $10 million for 2017, and $10 million for 2016.

## 8. Leases

We lease certain vehicles, land, buildings, equipment and miscellaneous other items through operating rental agreements with varying terms, provisions and expiration dates.

Lease expense recognized in the Consolidated Statements of Income was $18 million in 2018, $18 million in 2017, and $16 million in 2016. APS's lease expense was $17 million in 2018, $17 million in 2017, and $15 million in 2016. These amounts do not include purchased power lease contracts, discussed below.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Estimated future minimum lease payments for Pinnacle West’s and APS’s operating leases, excluding purchased power agreements, are approximately as follows (dollars in thousands):

| Year | Pinnacle West Consolidated | APS |
|---|---|---|
| 2019 | $ 13,747 | $ 13,411 |
| 2020 | 12,428 | 12,143 |
| 2021 | 9,478 | 9,282 |
| 2022 | 6,513 | 6,321 |
| 2023 | 5,359 | 5,171 |
| Thereafter | 42,236 | 40,656 |
| Total future lease commitments | $ 89,761 | $ 86,984 |

In 1986, APS entered into agreements with three separate lessor trust entities in order to sell and lease back interests in Palo Verde Unit 2 and related common facilities. These lessor trust entities have been deemed VIEs for which APS is the primary beneficiary. As the primary beneficiary, APS consolidated these lessor trust entities. The impacts of these sale leaseback transactions are excluded from our lease disclosures as lease accounting is eliminated upon consolidation. See Note 18 for a discussion of VIEs.

**Purchased Power Lease Contracts**

A purchased power contract may contain a lease for accounting purposes. This generally occurs when a purchased power contract designates a specific power plant from which the buyer purchases substantially all of the output and also meets other required lease accounting criteria. APS has certain purchased power contracts that contain lease arrangements. The future minimum lease payments due under these contracts are $54 million, all of which relate to 2019. Due to the inherent uncertainty associated with the reliability of the fuel source, payments under most renewable purchased power lease contracts are considered contingent rents and are excluded from future minimum lease payments. See Note 10 for additional information on our purchased power contract estimated commitments.

Operating lease cost for purchased power lease contracts was $47 million in 2018, $60 million in 2017 and $82 million in 2016. In addition, contingent rents for purchased power lease contracts was $109 million in 2018, $100 million in 2017, and $88 million in 2016. These costs are recorded in fuel and purchased power on the Consolidated Statements of Income, and are subject to recovery under the PSA or RES. See Note 3.

See Note 2 for a discussion of the new lease accounting standard we adopted on January 1, 2019.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 9. Jointly-Owned Facilities

APS shares ownership of some of its generating and transmission facilities with other companies. We are responsible for our share of operating costs which are included in the corresponding operating expenses on our Consolidated Statements of Income. We are also responsible for providing our own financing. Our share of operating expenses and utility plant costs related to these facilities is accounted for using proportional consolidation. The following table shows APS's interests in those jointly-owned facilities recorded on the Consolidated Balance Sheets at December 31, 2018 (dollars in thousands):

| | Percent Owned | | Plant in Service | Accumulated Depreciation | Construction Work in Progress |
|---|---|---|---|---|---|
| Generating facilities: | | | | | |
| Palo Verde Units 1 and 3 | 29.1% | | $1,887,729 | $1,095,878 | $ 25,185 |
| Palo Verde Unit 2 (a) | 16.8% | | 638,419 | 369,372 | 20,852 |
| Palo Verde Common | 28.0% | (b) | 752,300 | 277,414 | 39,995 |
| Palo Verde Sale Leaseback | | (a) | 351,050 | 245,275 | — |
| Four Corners Generating Station | 63.0% | | 1,466,579 | 544,308 | 23,430 |
| Cholla common facilities (c) | 50.5% | | 183,390 | 82,434 | 893 |
| Transmission facilities: | | | | | |
| ANPP 500kV System | 33.5% | (b) | 129,587 | 49,340 | 2,705 |
| Navajo Southern System | 26.7% | (b) | 82,046 | 30,464 | 284 |
| Palo Verde — Yuma 500kV System | 19.0% | (b) | 15,304 | 6,729 | 530 |
| Four Corners Switchyards | 63.1% | (b) | 68,707 | 15,436 | 1,334 |
| Phoenix — Mead System | 17.1% | (b) | 39,329 | 18,527 | 44 |
| Palo Verde — Rudd 500kV System | 50.0% | | 93,887 | 25,573 | 302 |
| Morgan — Pinnacle Peak System | 64.6% | (b) | 117,722 | 16,744 | — |
| Round Valley System | 50.0% | | 515 | 153 | — |
| Palo Verde — Morgan System | 87.9% | (b) | 219,292 | 6,660 | — |
| Hassayampa — North Gila System | 80.0% | | 142,541 | 9,805 | — |
| Cholla 500kV Switchyard | 85.7% | | 5,078 | 1,414 | 38 |
| Saguaro 500kV Switchyard | 60.0% | | 20,414 | 12,790 | — |
| Kyrene — Knox System | 50.0% | | 578 | 307 | — |

(a) See Note 18.

(b) Weighted-average of interests.

(c) PacifiCorp owns Cholla Unit 4 and APS operates the unit for PacifiCorp. The common facilities at Cholla are jointly-owned.

APS also has a 14% ownership in the Navajo Plant. In the second quarter of 2017, APS's remaining net book value of its interest was reclassified from property, plant and equipment to a regulatory asset. See "Navajo Plant" in Note 3 for more details.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 10. Commitments and Contingencies

### Palo Verde Generating Station

### Spent Nuclear Fuel and Waste Disposal

On December 19, 2012, APS, acting on behalf of itself and the participant owners of Palo Verde, filed a second breach of contract lawsuit against the DOE in the United States Court of Federal Claims ("Court of Federal Claims"). The lawsuit sought to recover damages incurred due to the DOE’s breach of the Contract for Disposal of Spent Nuclear Fuel and/or High Level Radioactive Waste ("Standard Contract") for failing to accept Palo Verde's spent nuclear fuel and high level waste from January 1, 2007 through June 30, 2011, as it was required to do pursuant to the terms of the Standard Contract and the Nuclear Waste Policy Act. On August 18, 2014, APS and the DOE entered into a settlement agreement, stipulating to a dismissal of the lawsuit and payment of $57.4 million by the DOE to the Palo Verde owners for certain specified costs incurred by Palo Verde during the period January 1, 2007 through June 30, 2011. APS’s share of this amount is $16.7 million. Amounts recovered in the lawsuit and settlement were recorded as adjustments to a regulatory liability and had no impact on the amount of reported net income. In addition, the settlement agreement, as amended, provides APS with a method for submitting claims and getting recovery for costs incurred through December 31, 2019.

APS has submitted four claims pursuant to the terms of the August 18, 2014 settlement agreement, for four separate time periods during July 1, 2011 through June 30, 2018. The DOE has approved and paid $74.2 million for these claims (APS’s share is $21.6 million). The amounts recovered were primarily recorded as adjustments to a regulatory liability and had no impact on reported net income. In accordance with the 2017 Rate Case Decision, this regulatory liability is being refunded to customers (see Note 3). APS's next claim pursuant to the terms of the August 18, 2014 settlement agreement was submitted to the DOE on October 31, 2018 in the amount of $10.2 million (APS's share is $3.0 million). This claim is pending DOE review.

### Nuclear Insurance

Public liability for incidents at nuclear power plants is governed by the Price-Anderson Nuclear Industries Indemnity Act ("Price-Anderson Act"), which limits the liability of nuclear reactor owners to the amount of insurance available from both commercial sources and an industry-wide retrospective payment plan. In accordance with the Price-Anderson Act, the Palo Verde participants are insured against public liability for a nuclear incident of up to approximately $14.1 billion per occurrence. Palo Verde maintains the maximum available nuclear liability insurance in the amount of $450 million, which is provided by American Nuclear Insurers ("ANI"). The remaining balance of approximately $13.6 billion of liability coverage is provided through a mandatory industry-wide retrospective premium program. If losses at any nuclear power plant covered by the program exceed the accumulated funds, APS could be responsible for retrospective premiums. The maximum retrospective premium per reactor under the program for each nuclear liability incident is approximately $137.6 million, subject to a maximum annual premium of approximately $20.5 million per incident. Based on APS's ownership interest in the three Palo Verde units, APS's maximum retrospective premium per incident for all three units is approximately $120.1 million, with a maximum annual retrospective premium of approximately $17.9 million.

The Palo Verde participants maintain insurance for property damage to, and decontamination of, property at Palo Verde in the aggregate amount of $2.8 billion. APS has also secured accidental outage insurance for a sudden and unforeseen accidental outage of any of the three units. The property damage, decontamination, and accidental outage insurance are provided by Nuclear Electric Insurance Limited

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

("NEIL"). APS is subject to retrospective premium adjustments under all NEIL policies if NEIL's losses in any policy year exceed accumulated funds. The maximum amount APS could incur under the current NEIL policies totals approximately $24.8 million for each retrospective premium assessment declared by NEIL's Board of Directors due to losses. In addition, NEIL policies contain rating triggers that would result in APS providing approximately $71.2 million of collateral assurance within 20 business days of a rating downgrade to non-investment grade. The insurance coverage discussed in this and the previous paragraph is subject to certain policy conditions, sublimits and exclusions.

## Fuel and Purchased Power Commitments and Purchase Obligations

APS is party to various fuel and purchased power contracts and purchase obligations with terms expiring between 2019 and 2043 that include required purchase provisions. APS estimates the contract requirements to be approximately $622 million in 2019; $555 million in 2020; $558 million in 2021; $563 million in 2022; $560 million in 2023; and $5.9 billion thereafter. However, these amounts may vary significantly pursuant to certain provisions in such contracts that permit us to decrease required purchases under certain circumstances. These amounts include estimated commitments relating to purchased power lease contracts, see Note 8.

Of the various fuel and purchased power contracts mentioned above, some of those contracts for coal supply include take-or-pay provisions. The current coal contracts with take-or-pay provisions have terms expiring through 2031.

The following table summarizes our estimated coal take-or-pay commitments (dollars in thousands):

| | Years Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2019 | 2020 | 2021 | 2022 | 2023 | Thereafter |
| Coal take-or-pay commitments (a) | $179,879 | $181,059 | $184,944 | $186,244 | $187,518 | $1,422,253 |

(a) Total take-or-pay commitments are approximately $2.3 billion. The total net present value of these commitments is approximately $1.7 billion.

APS may spend more to meet its actual fuel requirements than the minimum purchase obligations in our coal take-or-pay contracts. The following table summarizes actual amounts purchased under the coal contracts which include take-or-pay provisions for each of the last three years (dollars in thousands):

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Total purchases | $206,093 | $165,220 | $160,066 |

**Renewable Energy Credits**

APS has entered into contracts to purchase renewable energy credits to comply with the RES. APS estimates the contract requirements to be approximately $37 million in 2019; $36 million in 2020; $34 million in 2021; $31 million in 2022; $30 million in 2023; and $155 million thereafter. These amounts do not include purchases of renewable energy credits that are bundled with energy.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Coal Mine Reclamation Obligations

APS must reimburse certain coal providers for amounts incurred for final and contemporaneous coal mine reclamation. We account for contemporaneous reclamation costs as part of the cost of the delivered coal. We utilize site-specific studies of costs expected to be incurred in the future to estimate our final reclamation obligation. These studies utilize various assumptions to estimate the future costs. Based on the most recent reclamation studies, APS recorded an obligation for the coal mine final reclamation of approximately $213 million at December 31, 2018 and $216 million at December 31, 2017. Under our current coal supply agreements, APS expects to make payments for the final mine reclamation as follows: $32 million in 2019; $21 million in 2020; $21 million in 2021; $22 million in 2022; $24 million in 2023; and $167 million thereafter. Any amendments to current coal supply agreements may change the timing of the contribution. Portions of these funds will be held in an escrow account and distributed to certain coal providers under the terms of the applicable coal supply agreements.

### Superfund-Related Matters

The Comprehensive Environmental Response Compensation and Liability Act ("CERCLA" or "Superfund") establishes liability for the cleanup of hazardous substances found contaminating the soil, water or air. Those who released, generated, transported to, or disposed of hazardous substances at a contaminated site are among the parties who are potentially responsible ("PRPs"). PRPs may be strictly, and often are jointly and severally, liable for clean-up. On September 3, 2003, EPA advised APS that EPA considers APS to be a PRP in the Motorola 52nd Street Superfund Site, Operable Unit 3 ("OU3") in Phoenix, Arizona. APS has facilities that are within this Superfund site. APS and Pinnacle West have agreed with EPA to perform certain investigative activities of the APS facilities within OU3. In addition, on September 23, 2009, APS agreed with EPA and one other PRP to voluntarily assist with the funding and management of the site-wide groundwater remedial investigation and feasibility study ("RI/FS"). Based upon discussions between the OU3 working group parties and EPA, along with the results of recent technical analyses prepared by the OU3 working group to supplement the RI/FS for OU3, APS anticipates finalizing the RI/FS in the fall or winter of 2019. We estimate that our costs related to this investigation and study will be approximately $2 million. We anticipate incurring additional expenditures in the future, but because the overall investigation is not complete and ultimate remediation requirements are not yet finalized, at the present time expenditures related to this matter cannot be reasonably estimated.

On August 6, 2013, Roosevelt Irrigation District ("RID") filed a lawsuit in Arizona District Court against APS and 24 other defendants, alleging that RID’s groundwater wells were contaminated by the release of hazardous substances from facilities owned or operated by the defendants.  The lawsuit also alleges that, under Superfund laws, the defendants are jointly and severally liable to RID.  The allegations against APS arise out of APS’s current and former ownership of facilities in and around OU3.  As part of a state governmental investigation into groundwater contamination in this area, on January 25, 2015, ADEQ sent a letter to APS seeking information concerning the degree to which, if any, APS’s current and former ownership of these facilities may have contributed to groundwater contamination in this area.  APS responded to ADEQ on May 4, 2015. On December 16, 2016, two RID environmental and engineering contractors filed an ancillary lawsuit for recovery of costs against APS and the other defendants in the RID litigation. That same day, another RID service provider filed an additional ancillary CERCLA lawsuit against certain of the defendants in the main RID litigation, but excluded APS and certain other parties as named defendants. Because the ancillary lawsuits concern past costs allegedly incurred by these RID vendors, which were ruled unrecoverable directly by RID in November of 2016, the additional lawsuits do not increase APS's exposure or risk related to these matters.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On April 5, 2018, RID and the defendants in that particular litigation executed a settlement agreement, fully resolving RID's CERCLA claims concerning both past and future cost recovery. APS's share of this settlement was immaterial. In addition, the two environmental and engineering vendors voluntarily dismissed their lawsuit against APS and the other named defendants without prejudice. An order to this effect was entered on April 17, 2018. With this disposition of the case, the vendors may file their lawsuit again in the future. In addition, APS and certain other parties not named in the remaining RID service provider lawsuit may be brought into the litigation via third-party complaints filed by the current direct defendants. We are unable to predict the outcome of these matters; however, we do not expect the outcome to have a material impact on our financial position, results of operations or cash flows.

### Environmental Matters

APS is subject to numerous environmental laws and regulations affecting many aspects of its present and future operations, including air emissions of both conventional pollutants and greenhouse gases, water quality, wastewater discharges, solid waste, hazardous waste, and CCRs. These laws and regulations can change from time to time, imposing new obligations on APS resulting in increased capital, operating, and other costs. Associated capital expenditures or operating costs could be material. APS intends to seek recovery of any such environmental compliance costs through our rates, but cannot predict whether it will obtain such recovery. The following proposed and final rules involve material compliance costs to APS.

***Regional Haze Rules.*** APS has received the final rulemaking imposing new pollution control requirements on Four Corners and the Navajo Plant. EPA will require these plants to install pollution control equipment that constitutes BART to lessen the impacts of emissions on visibility surrounding the plants. In addition, EPA issued a final rule for Regional Haze compliance at Cholla that does not involve the installation of new pollution controls and that will replace an earlier BART determination for this facility. See below for details of the Cholla BART approval.

*Four Corners.* Based on EPA’s final standards, APS's 63% share of the cost of required controls for Four Corners Units 4 and 5 is approximately $400 million, the majority of which has already been incurred. In addition, APS and El Paso entered into an asset purchase agreement providing for the purchase by APS, or an affiliate of APS, of El Paso's 7% interest in Four Corners Units 4 and 5. 4CA purchased the El Paso interest on July 6, 2016. NTEC purchased the interest from 4CA on July 3, 2018. See "Four Corners Coal Supply Agreement - 4CA Matter" below for a discussion of the NTEC purchase. The cost of the pollution controls related to the 7% interest is approximately $45 million, which was assumed by NTEC through its purchase of the 7% interest.

*Navajo Plant.* APS estimates that its share of costs for upgrades at the Navajo Plant, based on EPA’s Federal Implementation Plan ("FIP"), could be up to approximately $200 million; however, given the future plans for the Navajo Plant, we do not expect to incur these costs. See "Navajo Plant" in Note 3 for information regarding future plans for the Navajo Plant.

*Cholla*. APS believed that EPA’s original 2012 final rule establishing controls constituting BART for Cholla, which would require installation of SCR controls, was unsupported and that EPA had no basis for disapproving Arizona’s State Implementation Plan ("SIP") and promulgating a FIP that was inconsistent with the state’s considered BART determinations under the regional haze program. In September 2014, APS met with EPA to propose a compromise BART strategy, whereby APS would permanently close Cholla Unit 2 and cease burning coal at Units 1 and 3 by the mid-2020s. (See Note 3 for details related to the resulting regulatory asset.) APS made the proposal with the understanding that additional emission control equipment is unlikely to be required in the future because retiring and/or converting the units as contemplated in the proposal is more

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

cost effective than, and will result in increased visibility improvement over, the BART requirements for oxides of nitrogen ("NOx") imposed through EPA's BART FIP. In early 2017, EPA approved a final rule incorporating APS's compromise proposal, which took effect for Cholla on April 26, 2017.

***Coal Combustion Waste.*** On December 19, 2014, EPA issued its final regulations governing the handling and disposal of CCR, such as fly ash and bottom ash. The rule regulates CCR as a non-hazardous waste under Subtitle D of the Resource Conservation and Recovery Act ("RCRA") and establishes national minimum criteria for existing and new CCR landfills and surface impoundments and all lateral expansions consisting of location restrictions, design and operating criteria, groundwater monitoring and corrective action, closure requirements and post closure care, and recordkeeping, notification, and internet posting requirements. The rule generally requires any existing unlined CCR surface impoundment that is contaminating groundwater above a regulated constituent’s groundwater protection standard to stop receiving CCR and either retrofit or close, and further requires the closure of any CCR landfill or surface impoundment that cannot meet the applicable performance criteria for location restrictions or structural integrity. Such closure requirements are deemed "forced closure" or "closure for cause" of unlined surface impoundments, and are the subject of recent regulatory and judicial activities described below.

On December 16, 2016, President Obama signed the Water Infrastructure Improvements for the Nation ("WIIN") Act into law, which contains a number of provisions requiring EPA to modify the self-implementing provisions of the Agency's current CCR rules under Subtitle D. Such modifications include new EPA authority to directly enforce the CCR rules through the use of administrative orders and providing states, like Arizona, where the Cholla facility is located, the option of developing CCR disposal unit permitting programs, subject to EPA approval. For facilities in states that do not develop state-specific permitting programs, EPA is required to develop a federal permit program, pending the availability of congressional appropriations. By contrast, for facilities located within the boundaries of Native American tribal reservations, such as the Navajo Nation, where the Navajo Plant and Four Corners facilities are located, EPA is required to develop a federal permit program regardless of appropriated funds.

ADEQ has initiated a process to evaluate how to develop a state CCR permitting program that would cover electric generating units ("EGUs"), including Cholla. While APS has been working with ADEQ on the development of this program, we are unable to predict when

Arizona will be able to finalize and secure EPA approval for a state-specific CCR permitting program. With respect to the Navajo Nation, APS has sought clarification as to when and how EPA would be initiating permit proceedings for facilities on the reservation, including Four Corners. We are unable to predict at this time when EPA will be issuing CCR management permits for the facilities on the Navajo Nation. At this time, it remains unclear how the CCR provisions of the WIIN Act will affect APS and its management of CCR.

Based upon utility industry petitions for EPA to reconsider the RCRA Subtitle D regulations for CCR, which were premised in part on the CCR provisions of the 2016 WIIN Act, on September 13, 2017 EPA agreed to evaluate whether to revise these federal CCR regulations. On July 17, 2018, EPA finalized a revision to its RCRA Subtitle D regulations for CCR, the "Phase I, Part I" revision to its CCR regulations, deferring for future action a number of other proposed changes contemplated in a March 1, 2018 proposal. For the final rule issued on July 17, 2018, EPA established nationwide health-based standards for certain constituents of CCR subject to groundwater corrective action and delayed the closure deadlines for certain unlined CCR surface impoundments by 18 months (for example, those disposal units required to undergo forced closure). These changes to the federal regulations governing CCR disposal are unlikely to have a material impact on APS. As for those aspects of the March 2018 rulemaking proposal for which EPA has yet to take final action, it remains unclear which specific provisions of the federal CCR rules will ultimately be modified, how they will be modified, or when such modification will occur.

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Pursuant to a June 24, 2016 order by the D.C. Circuit Court of Appeals in the litigation by industry- and environmental-groups challenging EPA's CCR regulations, EPA is required to complete a rulemaking proceeding in the near future concerning whether or not boron must be included on the list of groundwater constituents that might trigger corrective action under EPA's CCR rules. Simultaneously with the issuance of EPA's proposed modifications to the federal CCR rules in response to industry petitions, on March 1, 2018, EPA issued a proposed rule seeking comment as to whether or not boron should be included on this list. EPA is not required to take final action approving the inclusion of boron. Should EPA take final action adding boron to the list of groundwater constituents that might trigger corrective action, any resulting corrective action measures may increase APS's costs of compliance with the CCR rule at our coal-fired generating facilities. At this time APS cannot predict the eventual results of this rulemaking proceeding concerning boron.

On August 21, 2018, the D.C. Circuit Court issued its decision on the merits in this litigation. The Court upheld the legality of EPA's CCR regulations, though it vacated and remanded back to EPA a number of specific provisions, which are to be corrected in accordance with the Court's order. Among the issues affecting APS's management of CCR, the D.C. Circuit's decision vacated and remanded those provisions of the EPA CCR regulations that allow for the operation of unlined CCR surface impoundments, even where those unlined impoundments have not otherwise violated a regulatory location restriction or groundwater protection standard (i.e., otherwise triggering forced closure). At this time, it remains unclear how this D.C. Circuit Court decision will affect APS's operations or any financial impacts, as EPA has yet to take regulatory action on remand to revise its 2015 CCR regulations consistent with the Court's order.

Based on this decision, on December 17, 2018, certain environmental groups filed an emergency motion with the D.C. Circuit to either stay or summarily vacate EPA's July 17, 2018 final rule extending the closure-initiation deadline for certain unlined CCR surface impoundments until October 2020. In response, EPA filed a motion to remand but not vacate that deadline extension regulation. We cannot predict the outcome of the D.C. Circuit's consideration of these dueling motions, and whether or how such a ruling would affect APS's operations.

APS currently disposes of CCR in ash ponds and dry storage areas at Cholla and Four Corners. APS estimates that its share of incremental costs to comply with the CCR rule for Four Corners is approximately $22 million and its share of incremental costs to comply with the CCR rule for Cholla is approximately $20 million. The Navajo Plant currently disposes of CCR in a dry landfill storage area. APS estimates that its share of incremental costs to comply with the CCR rule for the Navajo Plant is approximately $1 million. Additionally, the CCR rule requires ongoing, phased groundwater monitoring. By October 17, 2017, electric utility companies that own or operate CCR disposal units, such as APS, must have collected sufficient groundwater sampling data to initiate a detection monitoring program. To the extent that certain threshold constituents are identified through this initial detection monitoring at levels above the CCR rule's standards, the rule required the initiation of an assessment monitoring program by April 15, 2018.

APS recently completed the statistical analyses for its CCR disposal units that triggered assessment monitoring. APS determined that several of its CCR disposal units at Cholla and Four Corners will need to undergo corrective action. In addition, all such units must cease operating and initiate closure by October of 2020. APS currently estimates that the additional incremental costs to complete this corrective action and closure work, along with the costs to develop replacement CCR disposal capacity, could be approximately $5 million for both Cholla and Four Corners. APS initiated an assessment of corrective measures on January 14, 2019, and anticipates completing this assessment during the summer of 2019. During this assessment, APS will gather additional groundwater data, solicit input from the public, host public hearings, and select remedies. As such, this $5 million cost estimate may change based upon APS's performance of the CCR rule's corrective action assessment process. Given uncertainties that may exist until we have fully completed the corrective

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action assessment process, we cannot predict any ultimate impacts to the Company; however, at this time we do not believe any potential change to the cost estimate would have a material impact on our financial position, results of operations or cash flows.

***Clean Power Plan.*** On June 2, 2014, EPA issued two proposed rules to regulate greenhouse gas ("GHG") emissions from modified and reconstructed EGUs pursuant to Section 111(b) of the Clean Air Act and existing fossil fuel-fired power plants pursuant to Clean Air Act Section 111(d). On August 3, 2015, EPA finalized carbon pollution standards for EGUs, the "Clean Power Plan". On October 10, 2017, EPA issued a proposal to repeal the Clean Power Plan and proposed replacement regulations on August 21, 2018. In addition, judicial challenges to the Clean Power Plan are pending before the D.C. Circuit, though that litigation is currently in abeyance while EPA develops regulatory action to potentially repeal and replace that regulation.

EPA's pending proposal to regulate carbon emissions from EGUs replaces the Clean Power Plan with standards that are based entirely upon measures that can be implemented to improve the heat rate of steam-electric power plants, specifically coal-fired EGUs. In contrast with the Clean Power Plan, EPA's proposed "Affordable Clean Energy Rule" would not involve utility-level generation dispatch shifting away from coal-fired generation and toward renewable energy resources and natural gas-fired combined cycle power plants. In addition, to address the New Source Review ("NSR") implications of power plant upgrades potentially necessary to achieve compliance with the proposed Affordable Clean Energy Rule standards, EPA also proposed to revise EPA's NSR regulations to more readily authorize the implementation of EGU efficiency upgrades.

We cannot predict the outcome of EPA's regulatory actions related to the August 2015 carbon pollution standards for EGU's, including any actions related to EPA's repeal proposal for the Clean Power Plan or additional rulemaking actions to approve the EPA's recently proposed Affordable Clean Energy Rule. In addition, we cannot predict whether the D.C. Circuit Court will continue to hold the litigation challenging the original Clean Power Plan in abeyance in light of EPA's repeal proposal, which is still pending.

Other environmental rules that could involve material compliance costs include those related to effluent limitations, the ozone national ambient air quality standard and other rules or matters involving the Clean Air Act, Clean Water Act, Endangered Species Act, RCRA, Superfund, the Navajo Nation, and water supplies for our power plants. The financial impact of complying with current and future environmental rules could jeopardize the economic viability of our coal plants or the willingness or ability of power plant participants to fund any required equipment upgrades or continue their participation in these plants. The economics of continuing to own certain resources, particularly our coal plants, may deteriorate, warranting early retirement of those plants, which may result in asset impairments. APS would seek recovery in rates for the book value of any remaining investments in the plants as well as other costs related to early retirement, but cannot predict whether it would obtain such recovery.

**Federal Agency Environmental Lawsuit Related to Four Corners**

On April 20, 2016, several environmental groups filed a lawsuit against OSM and other federal agencies in the District of Arizona in connection with their issuance of the approvals that extended the life of Four Corners and the adjacent mine. The lawsuit alleges that these federal agencies violated both the Endangered Species Act ("ESA") and the National Environmental Policy Act ("NEPA") in providing the federal approvals necessary to extend operations at the Four Corners Power Plant and the adjacent Navajo Mine past July 6, 2016. APS filed a motion to intervene in the proceedings, which was granted on August 3, 2016.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On September 15, 2016, NTEC, the company that owns the adjacent mine, filed a motion to intervene for the purpose of dismissing the lawsuit based on NTEC's tribal sovereign immunity. On September 11, 2017, the Arizona District Court issued an order granting NTEC's motion, dismissing the litigation with prejudice, and terminating the proceedings. On November 9, 2017, the environmental group plaintiffs appealed the district court order dismissing their lawsuit. Oral argument for this appeal has been scheduled for March 2019. We cannot predict whether this appeal will be successful and, if it is successful, the outcome of further district court proceedings.

### Four Corners National Pollutant Discharge Elimination System ("NPDES") Permit

On July 16, 2018, several environmental groups filed a petition for review before the EPA Environmental Appeals Board ("EAB") concerning the NPDES wastewater discharge permit for Four Corners, which was reissued on June 12, 2018. The environmental groups allege that the permit was reissued in contravention of several requirements under the Clean Water Act and did not contain required provisions concerning EPA's 2015 revised effluent limitation guidelines for steam-electric EGUs, 2014 existing-source regulations governing cooling-water intake structures, and effluent limits for surface seepage and subsurface discharges from coal-ash disposal facilities. To address certain of these issues through a reconsidered permit, EPA took action on December 19, 2018 to withdraw the NPDES permit reissued in June 2018. Withdrawal of the permit moots the EAB appeal, and EPA filed a motion to dismiss on that basis. EPA indicated that it anticipates proposing a replacement NPDES permit by March 2019 and, depending on the extent of public comments concerning that proposal, taking final action on a new NPDES permit by June 2019. At this time, we cannot predict the outcome of EPA's reconsideration of the NPDES permit and whether reconsideration will have a material impact on our financial position, results of operations or cash flows.

### Four Corners Coal Supply Agreement

### Arbitration

On June 13, 2017, APS received a Demand for Arbitration from NTEC in connection with the Coal Supply Agreement, dated December 30, 2013, under which NTEC supplies coal to APS and the other Four Corners owners (collectively, the "Buyer") for use at the Four Corners Power Plant (the "2016 Coal Supply Agreement"). NTEC was originally seeking a declaratory judgment to support its interpretation of a provision regarding uncontrollable forces in the agreement that relates to annual minimum quantities of coal to be purchased by the Buyer. NTEC also alleged a shortfall in the Buyer's purchases for the initial contract year of approximately $30 million. APS's share of this amount is approximately$17 million. On September 20, 2017, NTEC amended its Demand for Arbitration, removing its request for a declaratory judgment and at such time was only seeking relief for the alleged shortfall in the Buyer's purchases for the initial contract year.

On June 29, 2018, the parties settled the dispute for $45 million, which includes settlement for the initial contract year and the current contract year. APS's share of this amount is approximately $34 million. In connection with the settlement, the parties amended the 2016 Coal Supply Agreement, including modifying the provisions that gave rise to this dispute. (See "4CA Matter" below for additional matters agreed to between 4CA and NTEC in the settlement arrangement.) The arbitration was dismissed on July 9, 2018.

**Coal Advance Purchase**

On March 12, 2018, APS paid to NTEC approximately $24 million as an advance payment for APS's share of coal under the 2016 Coal Supply Agreement. The coal inventory purchased represents an amount that APS expects to use for its plant operations within the next year.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 4CA Matter

On July 6, 2016, 4CA purchased El Paso’s 7% interest in Four Corners. NTEC had the option to purchase the 7% interest within a certain timeframe pursuant to an option granted to NTEC. On December 29, 2015, NTEC provided notice of its intent to exercise the option. The purchase did not occur during the originally contemplated timeframe. Concurrent with the settlement of the 2016 Coal Supply Agreement matter described above, NTEC and 4CA agreed to allow for the purchase by NTEC of the 7% interest, consistent with the option. On June 29, 2018, 4CA and NTEC entered into an asset purchase agreement providing for the sale to NTEC of 4CA's 7% interest in Four Corners. Completion of the sale was subject to the receipt of approval by FERC, which was received on July 2, 2018, and the sale transaction closed on July 3, 2018. NTEC purchased the 7% interest at 4CA’s book value, approximately $70 million, and will pay 4CA the purchase price over a period of four years pursuant to a secured interest-bearing promissory note. In connection with the sale, Pinnacle West guaranteed certain obligations that NTEC will have to the other owners of Four Corners, such as NTEC's 7% share of capital expenditures and operating and maintenance expenses. Pinnacle West's guarantee is secured by a portion of APS's payments to be owed to NTEC under the 2016 Coal Supply Agreement.
The 2016 Coal Supply Agreement contained alternate pricing terms for the 7% interest in the event NTEC did not purchase the interest. Until the time that NTEC purchased the 7% interest, the alternate pricing provisions were applicable to 4CA as the holder of the 7% interest. These terms included a formula under which NTEC must make certain payments to 4CA for reimbursement of operations and maintenance costs and a specified rate of return, offset by revenue generated by 4CA’s power sales. Such payments are due to 4CA at the end of each calendar year. A $10 million payment was due to 4CA at December 31, 2017, which NTEC satisfied by directing to 4CA a prepayment from APS of a portion of a future mine reclamation obligation. The balance of the amount under this formula due December 31, 2018 for calendar year 2017 is approximately $20 million, which was paid to 4CA on December 14, 2018. The balance of the amount under this formula at December 31, 2018 for calendar year 2018 (up to the date that NTEC purchased the 7% interest) is approximately $10 million, which is due to 4CA at December 31, 2019.

### Financial Assurances

In the normal course of business, we obtain standby letters of credit and surety bonds from financial institutions and other third parties. These instruments guarantee our own future performance and provide third parties with financial and performance assurance in the event we do not perform. These instruments support certain commodity contract collateral obligations and other transactions. As of December 31, 2018, standby letters of credit totaled $0.2 million and will expire in 2019. As of December 31, 2018, surety bonds expiring through 2019 totaled $17 million. The underlying liabilities insured by these instruments are reflected on our balance sheets, where applicable. Therefore, no additional liability is reflected for the letters of credit and surety bonds themselves.

We enter into agreements that include indemnification provisions relating to liabilities arising from or related to certain of our agreements. Most significantly, APS has agreed to indemnify the equity participants and other parties in the Palo Verde sale leaseback transactions with respect to certain tax matters. Generally, a maximum obligation is not explicitly stated in the indemnification provisions and, therefore, the overall maximum amount of the obligation under such indemnification provisions cannot be reasonably estimated. Based on historical experience and evaluation of the specific indemnities, we do not believe that any material loss related to such indemnification provisions is likely.

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Pinnacle West has issued parental guarantees and has provided indemnification under certain surety bonds for APS which were not material at December 31, 2018. Since July 6, 2016, Pinnacle West has issued five parental guarantees for 4CA relating to payment obligations arising from 4CA's acquisition of El Paso's 7% interest in Four Corners, and pursuant to the Four Corners participation agreement payment obligations arising from 4CA's ownership interest in Four Corners, four of which terminated following the sale of 4CA's 7% interest to NTEC. (See "Four Corners Coal Supply Agreement - 4CA Matter" above for information related to this sale.)

In connection with the sale of 4CA's 7% interest to NTEC, Pinnacle West is guaranteeing certain obligations that NTEC will have to the other owners of Four Corners. (See "Four Corners Coal Supply Agreement - 4CA Matter" above for information related to this guarantee.) A maximum obligation is not explicitly stated in the guarantee and, therefore, the overall maximum amount of the obligation under such guarantee cannot be reasonably estimated; however, we consider the fair value of this guarantee to be immaterial.

### 11. Asset Retirement Obligations

In 2018, APS recognized an ARO for the removal of hazardous waste containing solar panels at all of our utility scale solar plants, which resulted in an increase to the ARO in the amount of $14 million. In addition, due to the sale of 4CA assets to NTEC in 2018 (see Note 10 for more information on 4CA matters) there was a decrease to the ARO of $9 million. APS recognized an ARO of $7 million for rooftop solar removals in accordance with the obligations included in the customer contracts, which requires APS to remove the panels at the end of the contract life and includes the costs for the disposal of hazardous materials in accordance with environmental regulations. Finally, APS has other ARO adjustments resulting in a net decrease of $1 million.

In 2017, APS received a new decommissioning study for the Navajo Plant. This resulted in an increase to the ARO in the amount of $22 million, an increase in regulatory asset of $2 million and a reduction of the regulatory liability of $20 million.

The following table shows the change in our asset retirement obligations for 2018 and 2017 (dollars in thousands):

| | 2018 | 2017 |
|---|---|---|
| Asset retirement obligations at the beginning of year | $679,529 | $624,475 |
| Changes attributable to: | | |
| Accretion expense | 36,876 | 33,104 |
| Settlements | (9,726 ) | — |
| Estimated cash flow revisions | 2,002 | 21,950 |
| Newly incurred or acquired obligations | 17,864 | — |
| Asset retirement obligations at the end of year | $726,545 | $679,529 |

In accordance with regulatory accounting, APS accrues removal costs for its regulated utility assets, even if there is no legal obligation for removal. See detail of regulatory liabilities in Note 3.

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## 12. Selected Quarterly Financial Data (Unaudited)

Consolidated quarterly financial information for 2018 and 2017 is provided in the tables below (dollars in thousands, except per share amounts). Weather conditions cause significant seasonal fluctuations in our revenues; therefore, results for interim periods do not necessarily represent results expected for the year.

| | **2018 Quarter Ended** | | | | **2018** |
|---|---|---|---|---|---|
| | **March 31,** | **June 30,** | **September 30,** | **December 31,** | **Total** |
| Operating revenues | $692,714 | $974,123 | $1,268,034 | $756,376 | $3,691,247 |
| Operations and maintenance | 265,682 | 268,397 | 246,545 | 256,120 | 1,036,744 |
| Operating income | 31,334 | 242,162 | 433,307 | 66,884 | 773,687 |
| Income taxes | (1,265) | 44,039 | 84,333 | 6,795 | 133,902 |
| Net income | 8,094 | 171,612 | 319,885 | 30,949 | 530,540 |
| Net income attributable to common shareholders | 3,221 | 166,738 | 315,012 | 26,076 | 511,047 |
| **Earnings Per Share:** | | | | | |
| Net income attributable to common shareholders — Basic | $0.03 | $1.49 | $2.81 | $0.23 | $4.56 |
| Net income attributable to common shareholders — Diluted | 0.03 | 1.48 | 2.80 | 0.23 | 4.54 |

| | **2017 Quarter Ended** | | | | **2017** |
|---|---|---|---|---|---|
| | **March 31,** | **June 30,** | **September 30,** | **December 31,** | **Total** |
| Operating revenues | $677,728 | $944,587 | $1,183,322 | $759,659 | $3,565,296 |
| Operations and maintenance | 226,071 | 220,985 | 230,839 | 271,212 | 949,107 |
| Operating income | 67,411 | 297,257 | 459,548 | 85,547 | 909,763 |
| Income taxes | 4,211 | 88,967 | 144,319 | 20,775 | 258,272 |
| Net income | 28,185 | 172,317 | 280,945 | 26,502 | 507,949 |
| Net income attributable to common shareholders | 23,312 | 167,443 | 276,072 | 21,629 | 488,456 |
| **Earnings Per Share:** | | | | | |
| Net income attributable to common shareholders — Basic | $0.21 | $1.50 | $2.47 | $0.19 | $4.37 |
| Net income attributable to common shareholders — Diluted | 0.21 | 1.49 | 2.46 | 0.19 | 4.35 |

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Selected Quarterly Financial Data (Unaudited) - APS

APS's quarterly financial information for 2018 and 2017 is as follows (dollars in thousands):

| | 2018 Quarter Ended | | | | 2018 |
|---|---|---|---|---|---|
| | March 31, | June 30, | September 30, | December 31, | Total |
| Operating revenues | $692,006 | $971,963 | $1,267,997 | $756,376 | $3,688,342 |
| Operations and maintenance | 254,601 | 251,999 | 226,346 | 236,281 | 969,227 |
| Operating income | 37,878 | 251,590 | 453,547 | 86,753 | 829,768 |
| Net income attributable to common shareholder | 9,599 | 177,825 | 338,366 | 44,475 | 570,265 |

| | 2017 Quarter Ended | | | | 2017 |
|---|---|---|---|---|---|
| | March 31, | June 30, | September 30, | December 31, | Total |
| Operating revenues | $677,589 | $943,406 | $1,178,846 | $757,811 | $3,557,652 |
| Operations and maintenance | 219,008 | 215,775 | 222,374 | 260,826 | 917,983 |
| Operating income | 70,269 | 296,700 | 465,658 | 91,912 | 924,539 |
| Net income attributable to common shareholder | 23,162 | 169,108 | 284,256 | 27,783 | 504,309 |

## 13. Fair Value Measurements

We classify our assets and liabilities that are carried at fair value within the fair value hierarchy. This hierarchy ranks the quality and reliability of the inputs used to determine fair values, which are then classified and disclosed in one of three categories. The three levels of the fair value hierarchy are:

Level 1 — Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 — Other significant observable inputs, including quoted prices in active markets for similar assets or liabilities; quoted prices in markets that are not active, and model-derived valuations whose inputs are observable (such as yield curves).

Level 3 — Valuation models with significant unobservable inputs that are supported by little or no market activity. Instruments in this category include long-dated derivative transactions where valuations are unobservable due to the length of the transaction, options, and transactions in locations where observable market data does not exist. The valuation models we employ utilize spot prices, forward prices, historical market data and other factors to forecast future prices.

Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Thus, a valuation may be classified in Level 3 even though the valuation may include significant inputs that are readily observable. We maximize the use of observable inputs and minimize the use of unobservable inputs. We rely primarily on the market approach of using prices and other market information for identical and/or comparable assets and liabilities. If market data is not readily available, inputs may reflect our own assumptions about the inputs market participants would use. Our assessment of the inputs and the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of fair value assets and liabilities as well as their placement within the fair value hierarchy levels. We assess whether a market is active by obtaining observable broker quotes, reviewing actual market activity, and assessing the volume of transactions. We consider broker quotes observable inputs when the quote is

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

binding on the broker, we can validate the quote with market activity, or we can determine that the inputs the broker used to arrive at the quoted price are observable.

Certain instruments have been valued using the concept of Net Asset Value ("NAV"), as a practical expedient. These instruments are typically structured as investment companies offering shares or units to multiple investors for the purpose of providing a return. These instruments are similar to mutual funds; however, their NAV is generally not published and publicly available, nor are these instruments traded on an exchange. Instruments valued using NAV, as a practical expedient are included in our fair value disclosures however, in accordance with GAAP are not classified within the fair value hierarchy levels.

### Recurring Fair Value Measurements

We apply recurring fair value measurements to cash equivalents, derivative instruments, and investments held in the nuclear decommissioning trust and other special use funds. On an annual basis we apply fair value measurements to plan assets held in our retirement and other benefit plans.  See Note 7 for fair value discussion of plan assets held in our retirement and other benefit plans.

***Cash Equivalents***

Cash equivalents represent certain investments in money market funds that are valued using quoted prices in active markets.

***Risk Management Activities — Derivative Instruments***

Exchange traded commodity contracts are valued using unadjusted quoted prices.  For non-exchange traded commodity contracts, we calculate fair value based on the average of the bid and offer price, discounted to reflect net present value.  We maintain certain valuation adjustments for a number of risks associated with the valuation of future commitments.  These include valuation adjustments for liquidity and credit risks.  The liquidity valuation adjustment represents the cost that would be incurred if all unmatched positions were closed out or hedged.  The credit valuation adjustment represents estimated credit losses on our net exposure to counterparties, taking into account netting agreements, expected default experience for the credit rating of the counterparties and the overall diversification of the portfolio.  We maintain credit policies that management believes minimize overall credit risk.

Certain non-exchange traded commodity contracts are valued based on unobservable inputs due to the long-term nature of contracts, characteristics of the product, or the unique location of the transactions. Our long-dated energy transactions consist of observable valuations for the near-term portion and unobservable valuations for the long-term portions of the transaction. We rely primarily on broker quotes to value these instruments. When our valuations utilize broker quotes, we perform various control procedures to ensure the quote has been developed consistent with fair value accounting guidance. These controls include assessing the quote for reasonableness by comparison against other broker quotes, reviewing historical price relationships, and assessing market activity. When broker quotes are not available, the primary valuation technique used to calculate the fair value is the extrapolation of forward pricing curves using observable market data for more liquid delivery points in the same region and actual transactions at more illiquid delivery points.

When the unobservable portion is significant to the overall valuation of the transaction, the entire transaction is classified as Level 3. Our classification of instruments as Level 3 is primarily reflective of the long-term nature of our energy transactions.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Our energy risk management committee, consisting of officers and key management personnel, oversees our energy risk management activities to ensure compliance with our stated energy risk management policies. We have a risk control function that is responsible for valuing our derivative commodity instruments in accordance with established policies and procedures. The risk control function reports to the chief financial officer's organization.

### Investments Held in Nuclear Decommissioning Trust and Other Special Use Funds

The nuclear decommissioning trust and other special use funds invest in fixed income and equity securities. Other special use funds include the coal reclamation escrow account and the active union medical trust. See Note 19 for additional discussion about our investment accounts.

We value investments in fixed income and equity securities using information provided by our trustees and escrow agent. Our trustees and escrow agent use pricing services that utilize the valuation methodologies described below to determine fair market value. We have internal control procedures designed to ensure this information is consistent with fair value accounting guidance. These procedures include assessing valuations using an independent pricing source, verifying that pricing can be supported by actual recent market transactions, assessing hierarchy classifications, comparing investment returns with benchmarks, and obtaining and reviewing independent audit reports on the trustees' and escrow agent's internal operating controls and valuation processes.

#### *Fixed Income Securities*

Fixed income securities issued by the U.S. Treasury are valued using quoted active market prices and are typically classified as Level 1. Fixed income securities issued by corporations, municipalities, and other agencies, including mortgage-backed instruments, are valued using quoted inactive market prices, quoted active market prices for similar securities, or by utilizing calculations which incorporate observable inputs such as yield curves and spreads relative to such yield curves. These fixed income instruments are classified as Level 2. Whenever possible, multiple market quotes are obtained which enables a cross-check validation. A primary price source is identified based on asset type, class, or issue of securities.

Fixed income securities may also include short-term investments in certificates of deposit, variable rate notes, time deposit accounts, U.S. Treasury and Agency obligations, U.S. Treasury repurchase agreements, commercial paper, and other short term instruments. These instruments are valued using active market prices or utilizing observable inputs described above.

***Equity Securities***

The nuclear decommissioning trust's equity security investments are held indirectly through commingled funds. The commingled funds are valued using the funds' NAV as a practical expedient. The funds' NAV is primarily derived from the quoted active market prices of the underlying equity securities held by the funds. We may transact in these commingled funds on a semi-monthly basis at the NAV. The commingled funds are maintained by a bank and hold investments in accordance with the stated objective of tracking the performance of the S&P 500 Index. Because the commingled funds' shares are offered to a limited group of investors, they are not considered to be traded in an active market. As these instruments are valued using NAV, as a practical expedient, they have not been classified within the fair value hierarchy.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The nuclear decommissioning trust and other special use funds may also hold equity securities that include exchange traded mutual funds and money market accounts for short-term liquidity purposes. These short-term, highly-liquid, investments are valued using active market prices.

### *Fair Value Tables*

The following table presents the fair value at December 31, 2018 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in thousands):

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Other | | Balance at December 31, 2018 |
|---|---|---|---|---|---|---|
| Assets | | | | | | |
| Cash equivalents | $ 1,200 | $— | $ — | $— | | $ 1,200 |
| Risk management activities — derivative instruments: | | | | | | |
| Commodity contracts | — | 3,140 | 2 | (2,029 ) | (a) | 1,113 |
| Nuclear decommissioning trust: | | | | | | |
| Equity securities | 5,203 | — | — | 2,148 | (b) | 7,351 |
| U.S. commingled equity funds | — | — | — | 396,805 | (c) | 396,805 |
| U.S. Treasury debt | 148,173 | — | — | — | | 148,173 |
| Corporate debt | — | 96,656 | — | — | | 96,656 |
| Mortgage-backed debt securities | — | 113,115 | — | — | | 113,115 |
| Municipal bonds | — | 79,073 | — | — | | 79,073 |
| Other fixed income | — | 9,961 | — | — | | 9,961 |
| Subtotal nuclear decommissioning trust | 153,376 | 298,805 | — | 398,953 | | 851,134 |
| Other special use funds: | | | | | | |
| Equity securities | 45,130 | — | — | 593 | (b) | 45,723 |
| U.S. Treasury debt | 173,310 | — | — | — | | 173,310 |
| Municipal bonds | — | 17,068 | — | — | | 17,068 |
| Subtotal other special use funds | 218,440 | 17,068 | — | 593 | | 236,101 |
| Total Assets | $ 373,016 | $ 319,013 | $ 2 | $ 397,517 | | $ 1,089,548 |
| Liabilities | | | | | | |
| Risk management activities — derivative instruments: | | | | | | |
| Commodity contracts | $ — | $ (52,696 ) | $ (8,216 ) | $ 875 | (a) | $ (60,037 ) |

(a) Represents counterparty netting, margin, and collateral. See Note 16.

(b) Represents net pending securities sales and purchases.

(c)

Valued using NAV as a practical expedient and, therefore, are not classified in the fair value hierarchy.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the fair value at December 31, 2017 of our assets and liabilities that are measured at fair value on a recurring basis (dollars in thousands):

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (a) (Level 3) | Other | | Balance at December 31, 2017 |
|---|---|---|---|---|---|---|
| Assets | | | | | | |
| Cash equivalents | $ 10,630 | $— | $— | $— | | $ 10,630 |
| Risk management activities — derivative instruments: | | | | | | |
| Commodity contracts | — | 5,683 | 1,036 | (4,737 ) | (b) | 1,982 |
| Nuclear decommissioning trust: | | | | | | |
| Cash and cash equivalents | 7,224 | — | — | 109 | (d) | 7,333 |
| U.S. commingled equity funds | — | — | — | 417,390 | (e) | 417,390 |
| U.S. Treasury debt | 127,662 | — | — | — | | 127,662 |
| Corporate debt | — | 114,007 | — | — | | 114,007 |
| Mortgage-backed debt securities | — | 111,874 | — | — | | 111,874 |
| Municipal bonds | — | 79,049 | — | — | | 79,049 |
| Other fixed income | — | 13,685 | — | — | | 13,685 |
| Subtotal nuclear decommissioning trust | 134,886 | 318,615 | — | 417,499 | | 871,000 |
| Other special use funds (c): | 455 | 31,562 | — | 525 | | 32,542 |
| Total Assets | $ 145,971 | $ 355,860 | $ 1,036 | $ 413,287 | | $ 916,154 |
| Liabilities | | | | | | |
| Risk management activities — derivative instruments: | | | | | | |
| Commodity contracts | $ — | $ (78,646 ) | $ (19,292 ) | $ 1,516 | (b) | $ (96,422 ) |

(a) Primarily consists of long-dated electricity contracts.

(b) Represents counterparty netting, margin, and collateral. See Note 16.

(c) Primarily consists of fixed income municipal bonds. Presented as coal reclamation escrow in 2017.

(d) Represents nuclear decommissioning trust net pending securities sales and purchases.

(e) Valued using NAV as a practical expedient and, therefore, are not classified in the fair value hierarchy.

### Fair Value Measurements Classified as Level 3

The significant unobservable inputs used in the fair value measurement of our energy derivative contracts include broker quotes that cannot be validated as an observable input primarily due to the long-term nature of the quote. Significant changes in these inputs in isolation would result in significantly higher or lower fair value measurements. Changes in our derivative contract fair values, including changes relating to unobservable inputs, typically will not impact net income due to regulatory accounting treatment (see Note 3).

Because our forward commodity contracts classified as Level 3 are currently in a net purchase position, we would expect price increases of the underlying commodity to result in increases in the net fair value of the

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

related contracts. Conversely, if the price of the underlying commodity decreases, the net fair value of the related contracts would likely decrease.

Other unobservable valuation inputs include credit and liquidity reserves which do not have a material impact on our valuations; however, significant changes in these inputs could also result in higher or lower fair value measurements.

The following tables provide information regarding our significant unobservable inputs used to value our risk management derivative Level 3 instruments at December 31, 2018 and December 31, 2017:

| | December 31, 2018 Fair Value (thousands) | | Valuation Technique | Significant Unobservable Input | Range | Weighted-Average |
|---|---|---|---|---|---|---|
| **Commodity Contracts** | **Assets** | **Liabilities** | | | | |
| Electricity: | | | | | | |
| Forward Contracts (a) | $— | $2,456 | Discounted cash flows | Electricity forward price (per MWh) | $17.88 - $37.03 | $ 26.10 |
| Natural Gas: | | | | | | |
| Forward Contracts (a) | 2 | 5,760 | Discounted cash flows | Natural gas forward price (per MMBtu) | $1.79 - $2.92 | $ 2.48 |
| Total | $2 | $8,216 | | | | |

(a) Includes swaps and physical and financial contracts.

| | December 31, 2017 Fair Value (thousands) | | Valuation Technique | Significant Unobservable Input | Range | Weighted-Average |
|---|---|---|---|---|---|---|
| **Commodity Contracts** | **Assets** | **Liabilities** | | | | |
| Electricity: | | | | | | |
| Forward Contracts (a) | $21 | $15,485 | Discounted cash flows | Electricity forward price (per MWh) | $18.51 - $38.75 | $ 27.89 |
| Natural Gas: | | | | | | |
| Forward Contracts (a) | 1,015 | 3,807 | Discounted cash flows | Natural gas forward price (per MMBtu) | $2.33 - $3.11 | $ 2.71 |
| Total | $1,036 | $19,292 | | | | |

(a) Includes swaps and physical and financial contracts.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table shows the changes in fair value for our risk management activities' assets and liabilities that are measured at fair value on a recurring basis using Level 3 inputs for the years ended December 31, 2018 and 2017 (dollars in thousands):

| Commodity Contracts | Year Ended December 31, 2018 | 2017 |
|---|---|---|
| Net derivative balance at beginning of period | $(18,256) | $(47,406) |
| Total net gains (losses) realized/unrealized: | | |
| Included in earnings | — | — |
| Included in OCI | — | 3 |
| Deferred as a regulatory asset or liability | (1,130) | (13,643) |
| Settlements | (787) | 5,834 |
| Transfers into Level 3 from Level 2 | (12,830) | (10,026) |
| Transfers from Level 3 into Level 2 | 24,789 | 46,982 |
| Net derivative balance at end of period | $(8,214) | $(18,256) |
| Net unrealized gains included in earnings related to instruments still held at end of period | $— | $— |

Transfers between levels in the fair value hierarchy shown in the table above reflect the fair market value at the beginning of the period and are triggered by a change in the lowest significant input as of the end of the period. We had no significant Level 1 transfers to or from any other hierarchy level. Transfers in or out of Level 3 are typically related to our long-dated energy transactions that extend beyond available quoted periods.

### Financial Instruments Not Carried at Fair Value

The carrying value of our short-term borrowings approximate fair value and are classified within Level 2 of the fair value hierarchy. See Note 6 for our long-term debt fair values. The NTEC note receivable related to the sale of 4CA's interest in Four Corners bears interest at 3.9% per annum and has a book value of $61 million as of December 31, 2018, as presented on the Consolidated Balance Sheets. The carrying amount is not materially different from the fair value of the note receivable and is classified within Level 3 of the fair value hierarchy. See Note 10 for more information on 4CA matters.

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 14. Earnings Per Share

The following table presents the calculation of Pinnacle West's basic and diluted earnings per share for continuing operations attributable to common shareholders for the years ended December 31, 2018, 2017 and 2016 (in thousands, except per share amounts):

| | **2018** | **2017** | **2016** |
|---|---|---|---|
| Net income attributable to common shareholders | $511,047 | $488,456 | $442,034 |
| Weighted average common shares outstanding — basic | 112,129 | 111,839 | 111,409 |
| Net effect of dilutive securities: | | | |
| Contingently issuable performance shares and restricted stock units | 421 | 528 | 637 |
| Weighted average common shares outstanding — diluted | 112,550 | 112,367 | 112,046 |
| Earnings per weighted-average common share outstanding | | | |
| Net income attributable to common shareholders - basic | $4.56 | $4.37 | $3.97 |
| Net Income attributable to common shareholders - diluted | $4.54 | $4.35 | $3.95 |

## 15. Stock-Based Compensation

Pinnacle West has incentive compensation plans under which stock-based compensation is granted to officers, key-employees, and non-officer members of the Board of Directors. Awards granted under the 2012 Long-Term Incentive Plan ("2012 Plan") may be in the form of stock grants, restricted stock units, stock units, performance shares, restricted stock, dividend equivalents, performance share units, performance cash, incentive and non-qualified stock options, and stock appreciation rights. The 2012 Plan authorizes up to 4.6 million common shares to be available for grant. As of December 31, 2018, 1.9 million common shares were available for issuance under the 2012 Plan. During 2018, 2017, and 2016, the Company granted awards in the form of restricted stock units, stock units, stock grants, and performance shares. Awards granted from 2007 to 2011 were issued under the 2007 Long-Term Incentive Plan ("2007 Plan"), and no new awards may be granted under the 2007 Plan.

### Stock-Based Compensation Expense and Activity

Compensation cost included in net income for stock-based compensation plans was $20 million in 2018, $21 million in 2017, and $19 million in 2016. The compensation cost capitalized is immaterial for all years. Income tax benefits related to stock-based compensation arrangements were $7 million in 2018, $15 million in 2017, and $10 million in 2016.

As of December 31, 2018, there were approximately $9 million of unrecognized compensation costs related to nonvested stock-based compensation arrangements. We expect to recognize these costs over a weighted-average period of 2 years.

The total fair value of shares vested was $24 million in 2018, $22 million in 2017 and $22 million in 2016.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table is a summary of awards granted and the weighted-average grant date fair value for the three years ended 2018, 2017 and 2016:

| | Restricted Stock Units, Stock Grants, and Stock Units (a) | | | Performance Shares (b) | | |
|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | 2018 | 2017 | 2016 |
| Units granted | 132,997 | 161,963 | 141,811 | 171,708 | 147,706 | 166,666 |
| Weighted-average grant date fair value | $77.51 | $72.60 | $67.34 | $76.56 | $78.99 | $66.60 |

(a) Units granted includes awards that will be cash settled of 66,252 in 2018, 67,599 in 2017, and 43,952 in 2016.
(b) Reflects the target payout level.

The following table is a summary of the status of non-vested awards as of December 31, 2018 and changes during the year:

| | Restricted Stock Units, Stock Grants, and Stock Units | | Performance Shares | |
|---|---|---|---|---|
| | Shares | Weighted-Average Grant Date Fair Value | Shares (b) | Weighted-Average Grant Date Fair Value |
| Nonvested at January 1, 2018 | 291,288 | $ 69.78 | 309,502 | $ 72.46 |
| Granted | 132,997 | 77.51 | 171,708 | 76.56 |
| Vested | (147,938) | 67.12 | (159,284) | 66.61 |
| Forfeited (c) | (5,356) | 73.42 | (9,542) | 73.34 |
| Nonvested at December 31, 2018 | 270,991 (a) | 74.39 | 312,384 | 77.67 |
| Vested Awards Outstanding at December 31, 2018 | 73,144 | | 159,284 | |

(a) Includes 148,131 of awards that will be cash settled.
(b) The nonvested performance shares are reflected at target payout level.
(c) We account for forfeitures as they occur.

Share-based liabilities paid relating to restricted stock units were $4 million, $4 million and $3 million in 2018, 2017 and 2016, respectively. This includes cash used to settle restricted stock units of $5 million, $4 million and $3 million in 2018, 2017 and 2016, respectively. Restricted stock units that are cash settled are classified as liability awards. All performance shares are classified as equity awards.

### Restricted Stock Units, Stock Grants, and Stock Units

Restricted stock units are granted to officers and key employees. Restricted stock units typically vest and settle in equal annual installments over a 4-year period after the grant date. Vesting is typically dependent upon continuous service during the vesting period; however, awards granted to retirement-eligible employees will vest upon the employee's retirement. Awardees elect to receive payment in either 100% stock, 100% cash, or 50% in cash and 50% in stock. Restricted stock unit awards typically include a dividend equivalent feature. This feature allows each award to accrue dividend rights equal to the dividends they would have received had they directly owned the stock. Interest on dividend rights compounds quarterly. If the award is forfeited the employee is not entitled to the dividends on those shares.

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In December 2012, the Company granted a retention award of 50,617 performance-linked restricted stock units to the Chairman of the Board and Chief Executive Officer of Pinnacle West. This award vested on December 31, 2016, because he remained employed with the Company through that date. The Board did increase the number of awards that vested by 33,745 restricted stock units, payable in stock because certain performance requirements were met. In February 2017, 84,362 restricted stock units were released.

Compensation cost for restricted stock unit awards is based on the fair value of the award, with the fair value being the market price of our stock on the measurement date. Restricted stock unit awards that will be settled in cash are accounted for as liability awards, with compensation cost initially calculated on the date of grant using the Company's closing stock price, and remeasured at each balance sheet date. Restricted stock unit awards that will be settled in shares are accounted for as equity awards, with compensation cost calculated using the Company's closing stock price on the date of grant. Compensation cost is recognized over the requisite service period based on the fair value of the award.

Stock grants are issued to non-officer members of the Board of Directors. They may elect to receive the stock grant, or to defer receipt until a later date and receive stock units in lieu of the stock grant. The members of the Board of Directors who elect to defer may elect to receive payment in either 100% stock, 100% cash, or 50% in cash and 50% in stock. Each stock unit is convertible to one share of stock. The stock units accrue dividend rights, equal to the amount of dividends the Directors would have received had they directly owned stock equal to the number of vested restricted stock units or stock units from the date of grant to the date of payment, plus interest compounded quarterly. The dividends and interest are paid, based on the Director's election, in either stock, cash, or 50% in cash and 50% in stock.

## Performance Share Awards

Performance share awards are granted to officers and key employees. The awards contain two separate performance criteria that affect the number of shares that may be received if after the end of a 3-year performance period the performance criteria are met. For the first criteria, the number of shares that will vest is based on non-financial performance metrics (i.e., the metric component). The other criteria is based upon Pinnacle West's total shareholder return ("TSR") in relation to the TSR of other companies in a specified utility index (i.e., the TSR component). The exact number of shares issued will vary from 0% to

200% of the target award. Shares received include dividend rights paid in stock equal to the amount of dividends that recipients would have received had they directly owned stock, equal to the number of vested performance shares from the date of grant to the date of payment plus interest compounded quarterly. If the award is forfeited or if the performance criteria are not achieved, the employee is not entitled to the dividends on those shares.

Performance share awards are accounted for as equity awards, with compensation cost based on the fair value of the award on the grant date. Compensation cost relating to the metric component of the award is based on the Company's closing stock price on the date of grant, with compensation cost recognized over the requisite service period based on the number of shares expected to vest. Management evaluates the probability of meeting the metric component at each balance sheet date. If the metric component criteria are not ultimately achieved, no compensation cost is recognized relating to the metric component, and any previously recognized compensation cost is reversed. Compensation cost relating to the TSR component of the award is determined using a Monte Carlo simulation valuation model, with compensation cost recognized ratably over the requisite service period, regardless of the number of shares that actually vest.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 16. Derivative Accounting

Derivative financial instruments are used to manage exposure to commodity price and transportation costs of electricity, natural gas, coal, emissions allowances and interest rates. Risks associated with market volatility are managed by utilizing various physical and financial derivative instruments, including futures, forwards, options and swaps. As part of our overall risk management program, we may use derivative instruments to hedge purchases and sales of electricity and fuels. Derivative instruments that meet certain hedge accounting criteria may be designated as cash flow hedges and are used to limit our exposure to cash flow variability on forecasted transactions. The changes in market value of such instruments have a high correlation to price changes in the hedged transactions. Derivative instruments are also entered into for economic hedging purposes. While economic hedges may mitigate exposure to fluctuations in commodity prices, these instruments have not been designated as accounting hedges. Contracts that have the same terms (quantities, delivery points and delivery periods) and for which power does not flow are netted, which reduces both revenues and fuel and purchased power costs in our Consolidated Statements of Income, but does not impact our financial condition, net income or cash flows.

Our derivative instruments, excluding those qualifying for a scope exception, are recorded on the balance sheet as an asset or liability and are measured at fair value. See Note 13 for a discussion of fair value measurements. Derivative instruments may qualify for the normal purchases and normal sales scope exception if they require physical delivery and the quantities represent those transacted in the normal course of business. Derivative instruments qualifying for the normal purchases and sales scope exception are accounted for under the accrual method of accounting and excluded from our derivative instrument discussion and disclosures below.

For its regulated operations, APS defers for future rate treatment 100% of the unrealized gains and losses on derivatives pursuant to the PSA mechanism that would otherwise be recognized in income. Realized gains and losses on derivatives are deferred in accordance with the PSA to the extent the amounts are above or below the Base Fuel Rate (see Note 3). Gains and losses from derivatives in the following tables represent the amounts reflected in income before the effect of PSA deferrals.

As of December 31, 2018 and 2017, we had the following outstanding gross notional volume of derivatives, which represent both purchases and sales (does not reflect net position):

| Commodity | Unit of Measure | Quantity December 31, 2018 | December 31, 2017 |
|---|---|---|---|
| Power | GWh | 250 | 583 |
| Gas | Billion cubic feet | 218 | 240 |

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# COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## Gains and Losses from Derivative Instruments

The following table provides information about gains and losses from derivative instruments in designated cash flow accounting hedging relationships during the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

| Commodity Contracts | Financial Statement Location | Year Ended December 31, 2018 | 2017 | 2016 |
|---|---|---|---|---|
| Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion) | OCI — derivative instruments | $— | $(59) | $ 47 |
| Loss Reclassified from Accumulated OCI into Income (Effective Portion Realized) (a) | Fuel and purchased power (b) | (2,000) | (3,519) | (3,926) |

(a) During the years ended December 31, 2018, 2017, and 2016, we had no losses reclassified from accumulated OCI to earnings related to discontinued cash flow hedges.
(b) Amounts are before the effect of PSA deferrals.

During the next twelve months, we estimate that a net loss of $1.5 million before income taxes will be reclassified from accumulated OCI as an offset to the effect of market price changes for the related hedged transactions. In accordance with the PSA, most of these amounts will be recorded as either a regulatory asset or liability and have no immediate effect on earnings.

The following table provides information about gains and losses from derivative instruments not designated as accounting hedging instruments during the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

| Commodity Contracts | Financial Statement Location | Year Ended December 31, 2018 | 2017 | 2016 |
|---|---|---|---|---|
| Net Gain (Loss) Recognized in Income | Operating revenues | $(2,557) | $(1,192) | $771 |
| Net Gain (Loss) Recognized in Income | Fuel and purchased power (a) | (12,951) | (87,991) | 25,711 |
| Total | | $(15,508) | $(89,183) | $26,482 |

(a) Amounts are before the effect of PSA deferrals.

## Derivative Instruments in the Consolidated Balance Sheets

Our derivative transactions are typically executed under standardized or customized agreements, which include collateral requirements and, in the event of a default, would allow for the netting of positive and negative exposures associated with a single counterparty. Agreements that allow for the offsetting of positive and negative exposures associated with a single counterparty are considered master netting arrangements. Transactions with counterparties that have master netting arrangements are offset and reported net on the Consolidated Balance Sheets. Transactions that do not allow for offsetting of positive and negative positions are reported gross on the Consolidated Balance Sheets.

We do not offset a counterparty's current derivative contracts with the counterparty's non-current derivative contracts, although our master netting arrangements would allow current and non-current positions

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

to be offset in the event of a default. Additionally, in the event of a default, our master netting arrangements would allow for the offsetting of all transactions executed under the master netting arrangement. These types of transactions may include non-derivative instruments, derivatives qualifying for scope exceptions, trade receivables and trade payables arising from settled positions, and other forms of non-cash collateral (such as letters of credit). These types of transactions are excluded from the offsetting tables presented below.

As of December 31, 2017, we no longer have derivative instruments that are designated as cash flow hedging instruments.

The following tables provide information about the fair value of our risk management activities reported on a gross basis, and the impacts of offsetting as of December 31, 2018 and 2017. These amounts relate to commodity contracts and are located in the assets and liabilities from risk management activities lines of our Consolidated Balance Sheets.

| **As of December 31, 2018:** **(dollars in thousands)** | **Gross Recognized Derivatives (a)** | **Amounts Offset (b)** | **Net Recognized Derivatives** | **Other (c)** | **Amount Reported on Balance Sheet** |
|---|---|---|---|---|---|
| Current assets | $3,106 | $(2,149) | $957 | $156 | $1,113 |
| Investments and other assets | 36 | (36) | — | — | — |
| Total assets | 3,142 | (2,185) | 957 | 156 | 1,113 |
| | | | | | |
| Current liabilities | (36,345) | 2,149 | (34,196) | (1,310) | (35,506) |
| Deferred credits and other | (24,567) | 36 | (24,531) | — | (24,531) |
| Total liabilities | (60,912) | 2,185 | (58,727) | (1,310) | (60,037) |
| Total | $(57,770) | $— | $(57,770) | $(1,154) | $(58,924) |

(a) All of our gross recognized derivative instruments were subject to master netting arrangements.

(b) No cash collateral has been provided to counterparties, or received from counterparties, that is subject to offsetting.

(c) Represents cash collateral and cash margin that is not subject to offsetting. Amounts relate to non-derivative instruments, derivatives qualifying for scope exceptions, or collateral and margin posted in excess of the recognized derivative instrument. Includes cash collateral received from counterparties of $1,310 and cash margin provided to counterparties of $156.

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| As of December 31, 2017: (dollars in thousands) | Gross Recognized Derivatives (a) | Amounts Offset (b) | Net Recognized Derivatives | Other (c) | Amount Reported on Balance Sheet |
|---|---|---|---|---|---|
| Current assets | $5,427 | $(3,796) | $1,631 | $300 | $1,931 |
| Investments and other assets | 1,292 | (1,241) | 51 | — | 51 |
| Total assets | 6,719 | (5,037) | 1,682 | 300 | 1,982 |
| | | | | | |
| Current liabilities | (59,527) | 3,796 | (55,731) | (3,521) | (59,252) |
| Deferred credits and other | (38,411) | 1,241 | (37,170) | — | (37,170) |
| Total liabilities | (97,938) | 5,037 | (92,901) | (3,521) | (96,422) |
| Total | $(91,219) | $— | $(91,219) | $(3,221) | $(94,440) |

(a) All of our gross recognized derivative instruments were subject to master netting arrangements.

(b) No cash collateral has been provided to counterparties, or received from counterparties, that is subject to offsetting.

(c) Represents cash collateral and cash margin that is not subject to offsetting. Amounts relate to non-derivative instruments, derivatives qualifying for scope exceptions, or collateral and margin posted in excess of the recognized derivative instrument. Includes cash collateral received from counterparties of $3,521 and cash margin provided to counterparties of $300.

### Credit Risk and Credit Related Contingent Features

We are exposed to losses in the event of nonperformance or nonpayment by counterparties and have risk management contracts with many counterparties. As of December 31, 2018, Pinnacle West has no counterparties with positive exposures of greater than 10% of risk management assets. Our risk management process assesses and monitors the financial exposure of all counterparties. Despite the fact that the great majority of trading counterparties' debt is rated as investment grade by the credit rating agencies, there is still a possibility that one or more of these counterparties could default, resulting in a material impact on consolidated earnings for a given period. Counterparties in the portfolio consist principally of financial institutions, major energy companies, municipalities and local distribution companies. We maintain credit policies that we believe minimize overall credit risk to within acceptable limits. Determination of the credit quality of our counterparties is based upon a number of factors, including credit ratings and our evaluation of their financial condition. To manage credit risk, we employ collateral requirements and standardized agreements that allow for the netting of positive and negative exposures associated with a single counterparty. Valuation adjustments are established representing our estimated credit losses on our overall exposure to counterparties.

Certain of our derivative instrument contracts contain credit-risk-related contingent features including, among other things, investment grade credit rating provisions, credit-related cross-default provisions, and adequate assurance provisions. Adequate assurance provisions allow a counterparty with reasonable grounds for uncertainty to demand additional collateral based on subjective events and/or conditions. For those derivative instruments in a net liability position, with investment grade credit contingencies, the counterparties could demand additional collateral if our debt credit rating were to fall below investment grade (below BBB- for Standard & Poor’s or Fitch or Baa3 for Moody’s).

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table provides information about our derivative instruments that have credit-risk-related contingent features at December 31, 2018 (dollars in thousands):

| | December 31, 2018 |
|---|---|
| Aggregate fair value of derivative instruments in a net liability position | $60,912 |
| Cash collateral posted | — |
| Additional cash collateral in the event credit-risk related contingent features were fully triggered (a) | 56,876 |

(a) This amount is after counterparty netting and includes those contracts which qualify for scope exceptions, which are excluded from the derivative details above.

We also have energy related non-derivative instrument contracts with investment grade credit-related contingent features, which could also require us to post additional collateral of approximately $94 million if our debt credit ratings were to fall below investment grade.

## 17. Other Income and Other Expense

The following table provides detail of Pinnacle West's Consolidated other income and other expense for 2018, 2017 and 2016 (dollars in thousands):

| | 2018 | 2017 | 2016 |
|---|---|---|---|
| Other income: | | | |
| Interest income | $8,647 | $3,497 | $884 |
| Debt return on Four Corners SCR deferral (Note 3) | 16,153 | 354 | — |
| Miscellaneous | 96 | 155 | 17 |
| Total other income | $24,896 | $4,006 | $901 |
| Other expense: | | | |
| Non-operating costs | $(10,076) | $(11,749) | $(9,235) |
| Investment losses — net | (417) | (4,113) | (1,747) |
| Miscellaneous | (7,473) | (5,677) | (4,355) |
| Total other expense | $(17,966) | $(21,539) | $(15,337) |

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Other Income and Other Expense - APS

The following table provides detail of APS's other income and other expense for 2018, 2017 and 2016 (dollars in thousands):

| | 2018 | 2017 | 2016 |
|---|---|---|---|
| Other income: | | | |
| Interest income | $6,496 | $2,504 | $261 |
| Debt return on Four Corners SCR deferral (Note 3) | 16,153 | 354 | — |
| Miscellaneous | 97 | 155 | 10 |
| Total other income | $22,746 | $3,013 | $271 |
| Other expense: | | | |
| Non-operating costs | $(9,462) | $(10,825) | $(8,455) |
| Miscellaneous | (5,830) | (3,088) | (2,099) |
| Total other expense | $(15,292) | $(13,913) | $(10,554) |

## 18. Palo Verde Sale Leaseback Variable Interest Entities

In 1986, APS entered into agreements with three separate VIE lessor trust entities in order to sell and lease back interests in Palo Verde Unit 2 and related common facilities. APS will retain the assets through 2023 under one lease and 2033 under the other two leases. APS will be required to make payments relating to these leases of approximately $23 million annually for the period 2019 through 2023, and about $16 million annually for the period 2024 through 2033. At the end of the lease period, APS will have the option to purchase the leased assets at their fair market value, extend the leases for up to two years, or return the assets to the lessors.

The leases' terms give APS the ability to utilize the assets for a significant portion of the assets' economic life, and therefore provide APS with the power to direct activities of the VIEs that most significantly impact the VIEs' economic performance. Predominantly due to the lease terms, APS has been deemed the primary beneficiary of these VIEs and therefore consolidates the VIEs.

As a result of consolidation, we eliminate lease accounting and instead recognize depreciation expense, resulting in an increase in net income of $19 million for 2018, 2017 and 2016. The increase in net income is entirely attributable to the noncontrolling interests.

Income attributable to Pinnacle West shareholders is not impacted by the consolidation.

Our Consolidated Balance Sheets at December 31, 2018 and December 31, 2017 include the following amounts relating to the VIEs (dollars in thousands):

| | **December 31, 2018** | **December 31, 2017** |
|---|---|---|
| Palo Verde sale leaseback property, plant and equipment, net of accumulated depreciation | $105,775 | $109,645 |
| Equity-Noncontrolling interests | 125,790 | 129,040 |

Assets of the VIEs are restricted and may only be used for payment to the noncontrolling interest holders. These assets are reported on our consolidated financial statements.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

APS is exposed to losses relating to these VIEs upon the occurrence of certain events that APS does not consider reasonably likely to occur. Under certain circumstances (for example, the NRC issuing specified violation orders with respect to Palo Verde or the occurrence of specified nuclear events), APS would be required to make specified payments to the VIEs' noncontrolling equity participants and take title to the leased Unit 2 interests, which, if appropriate, may be required to be written down in value. If such an event were to occur during the lease periods, APS may be required to pay the noncontrolling equity participants approximately $297 million beginning in 2019, and up to $456 million over the lease extension term.

For regulatory ratemaking purposes, the agreements continue to be treated as operating leases and, as a result, we have recorded a regulatory asset relating to the arrangements.

### 19. Investments in Nuclear Decommissioning Trusts and Other Special Use Funds

We have investments in debt and equity securities held in Nuclear Decommissioning Trusts, Coal Reclamation Escrow Accounts, and an Active Union Employee Medical Account. Investments in debt securities are classified as available-for-sale securities. We record both debt and equity security investments at their fair value on our Consolidated Balance Sheets. See Note 13 for a discussion of how fair value is determined and the classification of the investments within the fair value hierarchy. The investments in each trust or account are restricted for use and are intended to fund specified costs and activities as further described for each fund below.

**Nuclear Decommissioning Trusts** - To fund the future costs APS expects to incur to decommission Palo Verde, APS established external decommissioning trusts in accordance with NRC regulations. Third-party investment managers are authorized to buy and sell securities per stated investment guidelines. The trust funds are invested in fixed income securities and equity securities. Earnings and proceeds from sales and maturities of securities are reinvested in the trusts. Because of the ability of APS to recover decommissioning costs in rates, and in accordance with the regulatory treatment, APS has deferred realized and unrealized gains and losses (including other-than-temporary impairments) in other regulatory liabilities.

**Coal Reclamation Escrow Accounts -** APS has investments restricted for the future coal mine reclamation funding related to Four Corners. This escrow account is primarily invested in fixed income securities. Earnings and proceeds from sales of securities are reinvested in the escrow account. Because of the ability of APS to recover coal reclamation costs in rates, and in accordance with the regulatory treatment, APS has deferred realized and unrealized gains and losses (including other-than-temporary impairments) in other regulatory liabilities. Activities relating to APS coal reclamation escrow account investments are included within the other special use funds in the table below.

**Active Union Employee Medical Account -** APS has investments restricted for paying active union employee medical costs. These investments were transferred from APS other postretirement benefit trust assets into the active union employee medical trust in January 2018 (see Note 7). These investments may be used to pay active union employee medical costs incurred in the current period and in future periods. The account is invested primarily in fixed income securities. In accordance with the ratemaking treatment, APS has deferred the unrealized gains and losses (including other-than-temporary impairments) in other regulatory assets. Activities relating to active union employee medical account investments are included within the other special use funds in the table below.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### *APS*

The following tables present the unrealized gains and losses based on the original cost of the investment and summarizes the fair value of APS's nuclear decommissioning trust and other special use fund assets at December 31, 2018 and December 31, 2017 (dollars in thousands):

| Investment Type: | December 31, 2018 Fair Value Nuclear Decommissioning Trusts | Other Special Use Funds | Total | | Total Unrealized Gains | Total Unrealized Losses |
|---|---|---|---|---|---|---|
| Equity Securities | $402,008 | $45,130 | $447,138 | | $222,147 | $(459) |
| Available for Sale-Fixed Income Securities | 446,978 | 190,378 | 637,356 | (a) | 8,634 | (6,778) |
| Other | 2,148 | 593 | 2,741 | (b) | — | — |
| Total | $851,134 | $236,101 | $1,087,235 | | $230,781 | $(7,237) |

(a) As of December 31, 2018, the amortized cost basis of these available-for-sale investments is $635 million

(b) Represents net pending securities sales and purchases.

| Investment Type: | December 31, 2017 Fair Value Nuclear Decommissioning Trusts | Other Special Use Funds | Total | | Total Unrealized Gains | Total Unrealized Losses |
|---|---|---|---|---|---|---|
| Equity Securities | $424,614 | $430 | $425,044 | | $248,623 | $— |
| Available for Sale-Fixed Income Securities | 446,277 | 29,439 | 475,716 | (a) | 11,537 | (2,996) |
| Other | 109 | 489 | 598 | (b) | — | — |
| Total | $871,000 | $30,358 | $901,358 | | $260,160 | $(2,996) |

(a) As of December 31, 2017, the amortized cost basis of these available-for-sale investments is $467 million.

(b) Represents net pending securities sales and purchases.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table sets forth APS's realized gains and losses relating to the sale and maturity of available-for-sale debt securities and equity securities, and the proceeds from the sale and maturity of these investment securities for the years ended December 31, 2018, 2017 and 2016 (dollars in thousands):

| | Year Ended December 31, | | |
|---|---|---|---|
| | Nuclear Decommissioning Trusts | Other Special Use Funds | Total |
| **2018** | | | |
| Realized gains | $6,679 | $ 1 | $6,680 |
| Realized losses | (13,552) | — | (13,552) |
| Proceeds from the sale of securities (a) | 554,385 | 98,648 | 653,033 |
| **2017** | | | |
| Realized gains | 21,813 | 17 | 21,830 |
| Realized losses | (13,146) | (9) | (13,155) |
| Proceeds from the sale of securities (a) | 542,246 | 4,093 | 546,339 |
| **2016** | | | |
| Realized gains | 11,213 | — | 11,213 |
| Realized losses | (10,106) | — | (10,106) |
| Proceeds from the sale of securities (a) | 633,410 | — | 633,410 |

(a) Proceeds are reinvested in the nuclear decommissioning trusts or other special use funds.

### Fixed Income Securities Contractual Maturities

The fair value of fixed income securities, summarized by contractual maturities, at December 31, 2018 is as follows (dollars in thousands):

| | Nuclear Decommissioning | Coal Reclamation Escrow Accounts | Active Union Medical Trust | Total |
|---|---|---|---|---|
| Less than one year | $ 26,819 | $ 21,237 | $39,966 | $88,022 |
| 1 year – 5 years | 97,566 | 15,658 | 104,128 | 217,352 |
| 5 years – 10 years | 128,379 | 2,511 | — | 130,890 |
| Greater than 10 years | 194,214 | 6,878 | — | 201,092 |
| Total | $ 446,978 | $ 46,284 | $144,094 | $637,356 |

## 20. Revenue

On January 1, 2018, we adopted new revenue guidance in ASU 2014-09 and related amendments. The new revenue guidance requires entities to recognize revenue when control of the promised good or service is transferred to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. We applied the new guidance using the modified retrospective method applied to contracts which were not completed as of January 1, 2018. The adoption of the new revenue guidance resulted in expanded disclosures but otherwise did not have a material impact on our financial statements. New revenue disclosures required by the standard are included below, and in Note 1. See Note 2 for additional information regarding the new accounting standard.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Sources of Revenue**

The following table provides detail of Pinnacle West's consolidated revenue disaggregated by revenue sources (dollars in thousands):

| | **Year Ended December 31, 2018** |
|---|---|
| Retail residential electric service | $1,867,370 |
| Retail non-residential electric service | 1,628,891 |
| Wholesale energy sales | 109,198 |
| Transmission services for others | 60,261 |
| Other sources | 25,527 |
| **Total operating revenues** | $3,691,247 |

We derive our revenues from contracts with customers primarily from sales of electricity to our regulated retail customers. Our retail electric services and tariff rates are regulated by the ACC. Revenues from wholesale energy sales and transmission services for others represent energy and transmission sales to wholesale customers. Our wholesale activities and tariff rates are regulated by the FERC.

**Revenue Activities**

Our revenues are primarily derived from activities that are classified as revenues from contracts with customers. This includes sales of electricity to our regulated retail customers and wholesale and transmission activities. Our revenues from contracts with customers for the year ended December 31, 2018 were $3,644 million.

We have certain revenues that do not meet the specific accounting criteria to be classified as revenues from contracts with customers. For the year ended December 31, 2018, our revenues that do not qualify as revenue from contracts with customers were $47 million. This relates primarily to certain regulatory cost recovery mechanisms that are considered alternative revenue programs. We recognize revenue associated with alternative revenue programs when specific events permitting recognition are completed. Certain amounts associated with alternative revenue programs will subsequently be billed to customers; however, we do not reclassify billed amounts into revenue from contracts with customers. See Note 3 for a discussion of our regulatory cost recovery mechanisms.

**Contract Assets and Liabilities from Contracts with Customers**

There were no material contract assets, contract liabilities, or deferred contract costs recorded on the Consolidated Balance Sheets as of December 31, 2018.

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## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 21. Changes in Accumulated Other Comprehensive Loss

The following table shows the changes in Pinnacle West's consolidated accumulated other comprehensive loss, including reclassification adjustments, net of tax, by component for the years ended December 31, 2018 and 2017 (dollars in thousands):

| | Pension and Other Postretirement Benefits | | Derivative Instruments | | Total |
|---|---|---|---|---|---|
| Balance December 31, 2016 | $ (39,070) | | $ (4,752) | | $(43,822) |
| OCI (loss) before reclassifications | (6,438) | | (35) | | (6,473) |
| Amounts reclassified from accumulated other comprehensive loss | 3,068 | (a) | 2,225 | (b) | 5,293 |
| Balance December 31, 2017 | (42,440) | | (2,562) | | (45,002) |
| OCI (loss) before reclassifications | 102 | | (78) | | 24 |
| Amounts reclassified from accumulated other comprehensive loss | 4,295 | (a) | 1,527 | (b) | 5,822 |
| Reclassification of income tax effect related to tax reform | (7,954) | | (598) | | (8,552) |
| Balance December 31, 2018 | $ (45,997) | | $ (1,711) | | $(47,708) |

(a) These amounts primarily represent amortization of actuarial loss, and are included in the computation of net periodic pension cost. See Note 7.

(b) These amounts represent realized gains and losses and are included in the computation of fuel and purchased power costs and are subject to the PSA. See Note 16.

### Changes in Accumulated Other Comprehensive Loss - APS

The following table shows the changes in APS's consolidated accumulated other comprehensive loss, including reclassification adjustments, net of tax, by component for the years ended December 31, 2018 and 2017 (dollars in thousands):

| | Pension and Other Postretirement Benefits | | Derivative Instruments | | Total |
|---|---|---|---|---|---|
| Balance December 31, 2016 | $ (20,671) | | $ (4,752) | | $(25,423) |
| OCI (loss) before reclassifications | (6,884) | | (35) | | (6,919) |
| Amounts reclassified from accumulated other comprehensive loss | 3,134 | (a) | 2,225 | (b) | 5,359 |
| Balance December 31, 2017 | (24,421) | | (2,562) | | (26,983) |
| OCI (loss) before reclassifications | (326) | | (78) | | (404) |
| Amounts reclassified from accumulated other comprehensive loss | 3,791 | (a) | 1,527 | (b) | 5,318 |
| Reclassification of income tax effect related to tax reform | (4,440) | | (598) | | (5,038) |
| Balance December 31, 2018 | $ (25,396) | | $ (1,711) | | $(27,107) |

(a) These amounts primarily represent amortization of actuarial loss, and are included in the computation of net periodic pension cost.  See Note 7.

(b) These amounts represent realized gains and losses and are included in the computation of fuel and purchased power costs and are subject to the PSA.  See Note 16.

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**PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY**
**SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT**
**CONDENSED STATEMENTS OF COMPREHENSIVE INCOME**
(dollars in thousands)

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Operating revenues | $— | $119 | $370 |
| Operating expenses | 53,844 | 24,591 | 26,573 |
| Operating loss | (53,844) | (24,472) | (26,203) |
| Other | | | |
| Equity in earnings of subsidiaries | 569,249 | 507,495 | 462,027 |
| Other expense | (3,202) | (2,422) | (1,622) |
| Total | 566,047 | 505,073 | 460,405 |
| Interest expense | 12,074 | 5,633 | 3,151 |
| Income before income taxes | 500,129 | 474,968 | 431,051 |
| Income tax benefit | (10,918) | (13,488) | (10,983) |
| Net income attributable to common shareholders | 511,047 | 488,456 | 442,034 |
| Other comprehensive income (loss) — attributable to common shareholders | 5,846 | (1,180) | 926 |
| Total comprehensive income — attributable to common shareholders | $516,893 | $487,276 | $442,960 |

See Combined Notes to Consolidated Financial Statements.

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**PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY**
**SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT**
**CONDENSED BALANCE SHEETS**
(dollars in thousands)

| | December 31, 2018 | 2017 |
|---|---|---|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | $41 | $41 |
| Accounts receivable | 99,989 | 93,554 |
| Income tax receivable | 32,737 | 19,124 |
| Other current assets | 1,502 | 267 |
| Total current assets | 134,269 | 112,986 |
| Investments and other assets | | |
| Investments in subsidiaries | 5,859,834 | 5,465,137 |
| Deferred income taxes | 5,243 | 54,352 |
| Other assets | 34,910 | 44,613 |
| Total investments and other assets | 5,899,987 | 5,564,102 |
| Total Assets | $6,034,256 | $5,677,088 |
| LIABILITIES AND EQUITY | | |
| Current liabilities | | |
| Accounts payable | 9,565 | 7,638 |
| Accrued taxes | 9,006 | 8,927 |
| Common dividends payable | 82,675 | 77,667 |
| Short-term borrowings | 76,400 | 95,400 |
| Other current liabilities | 19,215 | 17,417 |
| Total current liabilities | 196,861 | 207,049 |
| Long-term debt less current maturities (Note 6) | 448,796 | 298,421 |
| Pension liabilities | 17,766 | 20,758 |
| Other | 22,128 | 15,130 |
| Total deferred credits and other | 39,894 | 35,888 |
| COMMITMENTS AND CONTINGENCIES (SEE NOTES) | | |
| Common stock equity | | |
| Common stock | 2,629,440 | 2,609,181 |
| Accumulated other comprehensive loss | (47,708) | (45,002) |
| Retained earnings | 2,641,183 | 2,442,511 |
| Total Pinnacle West Shareholders' equity | 5,222,915 | 5,006,690 |
| Noncontrolling interests | 125,790 | 129,040 |
| Total Equity | 5,348,705 | 5,135,730 |
| Total Liabilities and Equity | $6,034,256 | $5,677,088 |

See Combined Notes to Consolidated Financial Statements.

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# PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
# SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT
# CONDENSED STATEMENTS OF CASH FLOWS

(dollars in thousands)

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Cash flows from operating activities | | | |
| Net income | $511,047 | $488,456 | $442,034 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Equity in earnings of subsidiaries — net | (569,249) | (507,495) | (462,027) |
| Depreciation and amortization | 76 | 76 | 85 |
| Deferred income taxes | 49,535 | (264) | (12,402) |
| Accounts receivable | (7,881) | (2,106) | 15,823 |
| Accounts payable | 1,967 | (11,162) | 10,402 |
| Accrued taxes and income tax receivables — net | (13,535) | (22,247) | 20,041 |
| Dividends received from subsidiaries | 316,000 | 296,800 | 239,300 |
| Other | 31,807 | 15,092 | 5,514 |
| Net cash flow provided by operating activities | 319,767 | 257,150 | 258,770 |
| Cash flows from investing activities | | | |
| Construction work in progress | — | — | (18,457) |
| Investments in subsidiaries | (142,796) | (178,027) | (19,242) |
| Repayments of loans from subsidiaries | 6,477 | 2,987 | 1,026 |
| Advances of loans to subsidiaries | (500) | (6,388) | (2,092) |
| Net cash flow used for investing activities | (136,819) | (181,428) | (38,765) |
| Cash flows from financing activities | | | |
| Issuance of long-term debt | 150,000 | 298,761 | — |
| Short-term debt borrowings under revolving credit facility | 20,000 | 58,000 | 40,000 |
| Short-term debt repayments under revolving credit facility | (32,000) | (32,000) | — |
| Commercial paper - net | (7,000) | 27,700 | 1,700 |
| Dividends paid on common stock | (308,892) | (289,793) | (274,229) |
| Repayment of long-term debt | — | (125,000) | — |
| Common stock equity issuance - net of purchases | (5,055) | (13,390) | (4,867) |
| Other | (1) | — | — |
| Net cash flow used for financing activities | (182,948) | (75,722) | (237,396) |
| Net decrease in cash and cash equivalents | — | — | (17,391) |
| Cash and cash equivalents at beginning of year | 41 | 41 | 17,432 |
| Cash and cash equivalents at end of year | $41 | $41 | $41 |

See Combined Notes to Consolidated Financial Statements.

## PINNACLE WEST CAPITAL CORPORATION HOLDING COMPANY
## NOTES TO FINANCIAL STATEMENTS OF HOLDING COMPANY

The Combined Notes to Consolidated Financial Statements in Part II, Item 8 should be read in conjunction with the Pinnacle West Capital Corporation Holding Company Financial Statements.

The Pinnacle West Capital Corporation Holding Company Financial Statements have been prepared to present the financial position, results of operations and cash flows of Pinnacle West Capital Corporation on a stand-alone basis as a holding company. Investments in subsidiaries are accounted for using the equity method.

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**PINNACLE WEST CAPITAL CORPORATION**
**SCHEDULE II — RESERVE FOR UNCOLLECTIBLES**
(dollars in thousands)

| Column A | Column B | Column C | | Column D | Column E |
|---|---|---|---|---|---|
| | | Additions | | | |
| Description | Balance at beginning of period | Charged to cost and expenses | Charged to other accounts | Deductions | Balance at end of period |
| Reserve for uncollectibles: | | | | | |
| 2018 | $ 2,513 | $ 10,870 | $ — | $ 9,314 | $ 4,069 |
| 2017 | 3,037 | 6,836 | — | 7,360 | 2,513 |
| 2016 | 3,125 | 4,025 | — | 4,113 | 3,037 |

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## ARIZONA PUBLIC SERVICE COMPANY
## SCHEDULE II — RESERVE FOR UNCOLLECTIBLES
(dollars in thousands)

| Column A | Column B | Column C | | Column D | Column E |
|---|---|---|---|---|---|
| | | Additions | | | |
| Description | Balance at beginning of period | Charged to cost and expenses | Charged to other accounts | Deductions | Balance at end of period |
| Reserve for uncollectibles: | | | | | |
| 2018 | $ 2,513 | $ 10,870 | $ — | $ 9,314 | $ 4,069 |
| 2017 | 3,037 | 6,836 | — | 7,360 | 2,513 |
| 2016 | 3,125 | 4,025 | — | 4,113 | 3,037 |

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## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## ITEM 9A. CONTROLS AND PROCEDURES

(a)Disclosure Controls and Procedures

The term “disclosure controls and procedures” means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act of 1934 (the “Exchange Act”) (15 U.S.C. 78a *et seq.*) is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to a company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Pinnacle West’s management, with the participation of Pinnacle West’s Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of Pinnacle West’s disclosure controls and procedures as of December 31, 2018. Based on that evaluation, Pinnacle West’s Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, Pinnacle West’s disclosure controls and procedures were effective.

APS’s management, with the participation of APS’s Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of APS’s disclosure controls and procedures as of December 31, 2018. Based on that evaluation, APS’s Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, APS’s disclosure controls and procedures were effective.

(b)Management’s Annual Reports on Internal Control Over Financial Reporting

Reference is made to “Management’s Report on Internal Control over Financial Reporting (Pinnacle West Capital Corporation)” in Item 8 of this report and “Management’s Report on Internal Control over Financial Reporting (Arizona Public Service Company)” in Item 8 of this report.

(c)Attestation Reports of the Registered Public Accounting Firm

Reference is made to “Report of Independent Registered Public Accounting Firm” in Item 8 of this report and “Report of Independent Registered Public Accounting Firm” in Item 8 of this report on the internal control over financial reporting of Pinnacle West and APS, respectively.

(d)Changes In Internal Control Over Financial Reporting

No change in Pinnacle West’s or APS’s internal control over financial reporting occurred during the fiscal quarter ended December 31, 2018 that materially affected, or is reasonably likely to materially affect, Pinnacle West’s or APS’s internal control over financial reporting.

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## ITEM 9B. OTHER INFORMATION

None.

# PART III

## ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE OF PINNACLE WEST

Reference is hereby made to “Information About Our Board and Corporate Governance,” “Proposal 1 — Election of Directors” and to “Section 16(a) Beneficial Ownership Reporting Compliance” in the Pinnacle West Proxy Statement relating to the Annual Meeting of Shareholders to be held on May 15, 2019 (the “2019 Proxy Statement”) and to the “Executive Officers of Pinnacle West” section in Part I of this report.

Pinnacle West has adopted a Code of Ethics for Financial Executives that applies to financial executives including Pinnacle West’s Chief Executive Officer, Chief Financial Officer, Chief Accounting Officer, Controller, Treasurer, and General Counsel, the President and Chief Operating Officer of APS and other persons designated as financial executives by the Chair of the Audit Committee. The Code of Ethics for Financial Executives is posted on Pinnacle West’s website (*www.pinnaclewest.com)*. Pinnacle West intends to satisfy the requirements under Item 5.05 of Form 8-K regarding disclosure of amendments to, or waivers from, provisions of the Code of Ethics for Financial Executives by posting such information on Pinnacle West’s website.

## ITEM 11. EXECUTIVE COMPENSATION

Reference is hereby made to “Directors’ Compensation,” “Executive Compensation,” and “Human Resources Committee Interlocks and Insider Participation” in the 2019 Proxy Statement.

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# ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Reference is hereby made to “Ownership of Pinnacle West Stock” in the 2019 Proxy Statement.

## Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth information as of December 31, 2018 with respect to the 2012 Plan and the 2007 Plan, under which our equity securities are outstanding or currently authorized for issuance.

### *Equity Compensation Plan Information*

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted-average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c) |
|---|---|---|---|
| Equity compensation plans approved by security holders | 1,350,003 | — | 1,862,883 |
| Equity compensation plans not approved by security holders | | — | |
| **Total** | 1,350,003 | — | 1,862,883 |

(a) This amount includes shares subject to outstanding performance share awards and restricted stock unit awards at the maximum amount of shares issuable under such awards. However, payout of the performance share awards is contingent on the Company reaching certain levels of performance during a three-year performance period. If the performance criteria for these awards are not fully satisfied, the award recipient will receive less than the maximum number of shares available under these grants and may receive nothing from these grants.

(b) The weighted-average exercise price in this column does not take performance share awards or restricted stock unit awards into account, as those awards have no exercise price.

(c) Awards under the 2012 Plan can take the form of options, stock appreciation rights, restricted stock, performance shares, performance share units, performance cash, stock grants, stock units, dividend equivalents, and restricted stock units. Additional shares cannot be awarded under the 2007 Plan. However, if an award under the 2012 Plan is forfeited, terminated or canceled or expires, the shares subject to such award, to the extent of the forfeiture, termination, cancellation or expiration, may be added back to the shares available for issuance under the 2012 Plan.

**Equity Compensation Plans Approved By Security Holders**

Amounts in column (a) in the table above include shares subject to awards outstanding under two equity compensation plans that were previously approved by our shareholders: (a) the 2007 Plan, which was approved by our shareholders at our 2007 annual meeting of shareholders and under which no new stock awards may be granted; and (b) the 2012 Plan, as amended, which was approved by our shareholders at our 2012 annual meeting of shareholders and the first amendment to the 2012 Plan was approved by our shareholders at our 2017 annual meeting of shareholders. See Note 15 of the Notes to Consolidated Financial Statements for additional information regarding these plans.

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### Equity Compensation Plans Not Approved by Security Holders

The Company does not have any equity compensation plans under which shares can be issued that have not been approved by the shareholders.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Reference is hereby made to “Information About Our Board and Corporate Governance” and “Related Party Transactions” in the 2019 Proxy Statement.

# ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

## Pinnacle West

Reference is hereby made to “Accounting and Auditing Matters — Audit Fees and — Pre-Approval Policies” in the 2019 Proxy Statement.

## APS

The following fees were paid to APS’s independent registered public accountants, Deloitte & Touche LLP, for the last two fiscal years:

| Type of Service | 2018 | 2017 |
|---|---|---|
| Audit Fees (1) | $2,342,455 | $2,212,137 |
| Audit-Related Fees (2) | 300,334 | 292,467 |

(1) The aggregate fees billed for services rendered for the audit of annual financial statements and for review of financial statements included in Reports on Form 10-Q.
(2) The aggregate fees billed for assurance and related services that are reasonably related to the performance of the audit or review of the financial statements and are not included in Audit Fees reported above, which primarily consist of fees for employee benefit plan audits performed in 2018 and 2017.

Pinnacle West’s Audit Committee pre-approves each audit service and non-audit service to be provided by APS’s registered public accounting firm. The Audit Committee has delegated to the Chair of the Audit Committee the authority to pre-approve audit and non-audit services to be performed by the independent public accountants if the services are not expected to cost more than $50,000. The Chair must report any pre-approval decisions to the Audit Committee at its next scheduled meeting. All of the services performed by Deloitte & Touche LLP for APS in 2018 were pre-approved by the Audit Committee or the Chair consistent with the pre-approval policy.

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# PART IV

## ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

### Financial Statements and Financial Statement Schedules

See the Index to Financial Statements and Financial Statement Schedule in Part II, Item 8.

### Exhibits Filed

The documents listed below are being filed or have previously been filed on behalf of Pinnacle West or APS and are incorporated herein by reference from the documents indicated and made a part hereof. Exhibits not identified as previously filed are filed herewith.

| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 3.1 | Pinnacle West | Articles of Incorporation, restated as of May 21, 2008 | 3.1 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File No. 1-8962 | 8/7/2008 |
| 3.2 | Pinnacle West | Pinnacle West Capital Corporation Bylaws, amended as of February 22, 2017 | 3.1 to Pinnacle West/APS February 28, 2017 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 2/28/2017 |
| 3.3 | APS | Articles of Incorporation, restated as of May 25, 1988 | 4.2 to APS's Form 18 Registration Nos. 33-33910 and 33-55248 by means of September 24, 1993 Form 8-K Report, File No. 1-4473 | 9/29/1993 |
| 3.3.1 | APS | Amendment to the Articles of Incorporation of Arizona Public Service Company, amended May 16, 2012 | 3.1 to Pinnacle West/APS May 22, 2012 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 5/22/2012 |
| 3.4 | APS | Arizona Public Service Company Bylaws, amended as of December 16, 2008 | 3.4 to Pinnacle West/APS December 31, 2008 Form 10-K, File No. 1-4473 | 2/20/2009 |
| 4.1 | Pinnacle West | Specimen Certificate of Pinnacle West Capital Corporation Common Stock, no par value | 4.1 to Pinnacle West June 20, 2017 Form 8-K Report, File No. 1-8962 | 6/20/2017 |
| 4.2 | | | | 1/11/1995 |

| | | | | |
|---|---|---|---|---|
| | Pinnacle West APS | Indenture dated as of January 1, 1995 among APS and The Bank of New York Mellon, as Trustee | 4.6 to APS's Registration Statement Nos. 33-61228 and 33-55473 by means of January 1, 1995 Form 8-K Report, File No. 1-4473 | |
| 4.2a | Pinnacle West APS | First Supplemental Indenture dated as of January 1, 1995 | 4.4 to APS's Registration Statement Nos. 33-61228 and 33-55473 by means of January 1, 1995 Form 8-K Report, File No. 1-4473 | 1/11/1995 |
| 4.3 | Pinnacle West APS | Indenture dated as of November 15, 1996 between APS and The Bank of New York, as Trustee | 4.5 to APS's Registration Statements Nos. 33-61228, 33-55473, 33-64455 and 333- 15379 by means of November 19, 1996 Form 8-K Report, File No. 1-4473 | 11/22/1996 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 4.3a | Pinnacle West APS | First Supplemental Indenture dated as of November 15, 1996 | 4.6 to APS's Registration Statements Nos. 33-61228, 33-55473, 33-64455 and 333-15379 by means of November 19, 1996 Form 8-K Report, File No. 1-4473 | 11/22/1996 |
| 4.3b | Pinnacle West APS | Second Supplemental Indenture dated as of April 1, 1997 | 4.10 to APS's Registration Statement Nos. 33-55473, 33-64455 and 333-15379 by means of April 7, 1997 Form 8-K Report, File No. 1-4473 | 4/9/1997 |
| 4.3c | Pinnacle West APS | Third Supplemental Indenture dated as of November 1, 2002 | 10.2 to Pinnacle West's March 31, 2003 Form 10-Q Report, File No. 1-8962 | 5/15/2003 |
| 4.4 | Pinnacle West | Indenture dated as of December 1, 2000 between the Company and The Bank of New York, as Trustee, relating to Senior Unsecured Debt Securities | 4.1 to Pinnacle West's Registration Statement No. 333-52476 | 12/21/2000 |
| 4.4a | Pinnacle West | Third Supplemental Indenture dated as of November 30, 2017 | 4.1 to Pinnacle West November 30, 2017 Form 8-K Report, File No. 1-8962 | 11/30/2017 |
| 4.5 | Pinnacle West | Indenture dated as of December 1, 2000 between the Company and The Bank of New York, as Trustee, relating to Subordinated Unsecured Debt Securities | 4.2 to Pinnacle West's Registration Statement No. 333-52476 | 12/21/2000 |
| 4.6 | Pinnacle West APS | Indenture dated as of January 15, 1998 between APS and The Bank of New York Mellon Trust Company N.A. (successor to JPMorgan Chase Bank, N.A., formerly known as The Chase Manhattan Bank), as Trustee | 4.10 to APS's Registration Statement Nos. 333-15379 and 333-27551 by means of January 13, 1998 Form 8-K Report, File No. 1-4473 | 1/16/1998 |
| 4.6a | Pinnacle West APS | Seventh Supplemental Indenture dated as of May 1, 2003 | 4.1 to APS's Registration Statement No. 333-90824 by means of May 7, 2003 Form 8-K Report, File No. 1-4473 | 5/9/2003 |
| 4.6b | Pinnacle West APS | Eighth Supplemental Indenture dated as of June 15, 2004 | 4.1 to APS's Registration Statement No. 333-106772 by means of June 24, 2004 Form 8-K Report, File No. 1-4473 | 6/28/2004 |
| 4.6c | Pinnacle West APS | Ninth Supplemental Indenture dated as of August 15, 2005 | 4.1 to APS's Registration Statements Nos. 333-106772 and 333-121512 by means of August 17, 2005 Form 8-K Report, File No. 1-4473 | 8/22/2005 |
| 4.6d | APS | | | 8/3/2006 |

| | | | | |
|---|---|---|---|---|
| | | Tenth Supplemental Indenture dated as of August 1, 2006 | 4.1 to APS's July 31, 2006 Form 8-K Report, File No. 1-4473 | |
| 4.6e | Pinnacle West APS | Eleventh Supplemental Indenture dated as of February 26, 2009 | 4.6e to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |
| 4.6f | Pinnacle West APS | Twelfth Supplemental Indenture dated as of August 25, 2011 | 4.6f to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |
| 4.6g | Pinnacle West APS | Thirteenth Supplemental Indenture dated as of January 13, 2012 | 4.6g to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 4.6h | Pinnacle West APS | Fourteenth Supplemental Indenture dated as of January 10, 2014 | 4.6h to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |
| 4.6i | Pinnacle West APS | Fifteenth Supplemental Indenture dated as of June 18, 2014 | 4.6i to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |
| 4.6j | Pinnacle West APS | Sixteenth Supplemental Indenture dated as of January 12, 2015 | 4.6j to Pinnacle West/APS 2014 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/20/2015 |
| 4.6k | Pinnacle West APS | Seventeenth Supplemental Indenture dated as of May 19, 2015 | 4.1 to Pinnacle West/APS May 14, 2015 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 5/19/2015 |
| 4.6l | Pinnacle West APS | Eighteenth Supplemental Indenture dated as of November 6, 2015 | 4.1 to Pinnacle West/APS November 3, 2015 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 11/6/2015 |
| 4.6m | Pinnacle West APS | Nineteenth Supplemental Indenture dated as of May 6, 2016 | 4.1 to Pinnacle West/APS May 3, 2016 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 5/6/2016 |
| 4.6n | Pinnacle West APS | Twentieth Supplemental Indenture dated as of September 20, 2016 | 4.1 to Pinnacle West/APS September 15, 2016 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 9/20/2016 |
| 4.6o | Pinnacle West APS | Twenty-First Supplemental Indenture dated as of September 11, 2017 | 4.1 to Pinnacle West/APS September 11, 2017 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 9/11/2017 |
| 4.6p | Pinnacle West APS | Twenty-Second Supplemental Indenture dated as of August 9, 2018 | 4.1 to Pinnacle West/APS August 9, 2018 Form 8-K Report, File Nos. 1-8962 and 1-4473 | 8/9/2018 |
| 4.7 | Pinnacle West | Second Amended and Restated Pinnacle West Capital Corporation Investors Advantage Plan dated as of June 23, 2004 | 4.4 to Pinnacle West’s June 23, 2004 Form 8-K Report, File No. 1-8962 | 8/9/2004 |
| 4.7a | Pinnacle West | Third Amended and Restated Pinnacle West Capital Corporation Investors Advantage Plan dated as of November 25, 2008 | 4.1 to Pinnacle West’s Form S-3 Registration Statement No. 333-155641, File No. 1-8962 | 11/25/2008 |

| | | | | |
|---|---|---|---|---|
| 4.8 | Pinnacle West | Agreement, dated March 29, 1988, relating to the filing of instruments defining the rights of holders of long-term debt not in excess of 10% of the Company's total assets | 4.1 to Pinnacle West's 1987 Form 10-K Report, File No. 1-8962 | 3/30/1988 |
| 4.8a | Pinnacle West APS | Agreement, dated March 21, 1994, relating to the filing of instruments defining the rights of holders of APS long-term debt not in excess of 10% of APS's total assets | 4.1 to APS's 1993 Form 10-K Report, File No. 1-4473 | 3/30/1994 |
| 10.1.1 | Pinnacle West APS | Two separate Decommissioning Trust Agreements (relating to PVGS Units 1 and 3, respectively), each dated July 1, 1991, between APS and Mellon Bank, N.A., as Decommissioning Trustee | 10.2 to APS's September 30, 1991 Form 10-Q Report, File No. 1-4473 | 11/14/1991 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.1.1a | Pinnacle West APS | Amendment No. 1 to Decommissioning Trust Agreement (PVGS Unit 1), dated as of December 1, 1994 | 10.1 to APS's 1994 Form 10-K Report, File No. 1-4473 | 3/30/1995 |
| 10.1.1b | Pinnacle West APS | Amendment No. 1 to Decommissioning Trust Agreement (PVGS Unit 3), dated as of December 1, 1994 | 10.2 to APS's 1994 Form 10-K Report, File No. 1-4473 | 3/30/1995 |
| 10.1.1c | Pinnacle West APS | Amendment No. 2 to APS Decommissioning Trust Agreement (PVGS Unit 1) dated as of July 1, 1991 | 10.4 to APS's 1996 Form 10-K Report , File No. 1-4473 | 3/28/1997 |
| 10.1.1d | Pinnacle West APS | Amendment No. 2 to APS Decommissioning Trust Agreement (PVGS Unit 3) dated as of July 1, 1991 | 10.6 to APS's 1996 Form 10-K Report, File No. 1-4473 | 3/28/1997 |
| 10.1.1e | Pinnacle West APS | Amendment No. 3 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of March 18, 2002 | 10.2 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962 | 5/15/2002 |
| 10.1.1f | Pinnacle West APS | Amendment No. 3 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of March 18, 2002 | 10.4 to Pinnacle West's March 2002 Form 10-Q Report, File No. 1-8962 | 5/15/2002 |
| 10.1.1g | Pinnacle West APS | Amendment No. 4 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of December 19, 2003 | 10.3 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962 | 3/15/2004 |
| 10.1.1h | Pinnacle West APS | Amendment No. 4 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of December 19, 2003 | 10.5 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962 | 3/15/2004 |
| 10.1.1i | Pinnacle West APS | Amendment No. 5 to the Decommissioning Trust Agreement (PVGS Unit 1), dated as of May 1, 2007 | 10.1 to Pinnacle West/APS March 31, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/9/2007 |
| 10.1.1j | Pinnacle West APS | Amendment No. 5 to the Decommissioning Trust Agreement (PVGS Unit 3), dated as of May 1, 2007 | 10.2 to Pinnacle West/APS March 31, 2007 Form 10-Q Report, File Nos. 1-8962 and 104473 | 5/9/2007 |
| 10.1.2 | Pinnacle West APS | Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2) dated as of January 31, 1992, among APS, Mellon Bank, N.A., as Decommissioning Trustee, and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee under two separate Trust Agreements, | 10.1 to Pinnacle West's 1991 Form 10-K Report, File No. 1-8962 | 3/26/1992 |

each with a separate Equity Participant, and as Lessor under two separate Facility Leases, each relating to an undivided interest in PVGS Unit 2

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.1.2a | Pinnacle West APS | First Amendment to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of November 1, 1992 | 10.2 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 10.1.2b | Pinnacle West APS | Amendment No. 2 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of November 1, 1994 | 10.3 to APS's 1994 Form 10-K Report, File No. 1-4473 | 3/30/1995 |
| 10.1.2c | Pinnacle West APS | Amendment No. 3 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of June 20, 1996 | 10.1 to APS's June 30, 1996 Form 10-Q Report, File No. 1-4473 | 8/9/1996 |
| 10.1.2d | Pinnacle West APS | Amendment No. 4 to Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2) dated as of December 16, 1996 | APS 10.5 to APS's 1996 Form 10-K Report, File No. 1-4473 | 3/28/1997 |
| 10.1.2e | Pinnacle West APS | Amendment No. 5 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of June 30, 2000 | 10.1 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962 | 5/15/2002 |
| 10.1.2f | Pinnacle West APS | Amendment No. 6 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of March 18, 2002 | 10.3 to Pinnacle West's March 31, 2002 Form 10-Q Report, File No. 1-8962 | 5/15/2002 |
| 10.1.2g | Pinnacle West APS | Amendment No. 7 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of December 19, 2003 | 10.4 to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962 | 3/15/2004 |
| 10.1.2h | Pinnacle West APS | Amendment No. 8 to the Amended and Restated Decommissioning Trust Agreement (PVGS Unit 2), dated as of April 1, 2007 | 10.1.2h to Pinnacle West's 2007 Form 10-K Report, File No. 1-8962 | 2/27/2008 |
| 10.2.1[b] | Pinnacle West APS | Arizona Public Service Company Deferred Compensation Plan, as restated, effective January 1, 1984, and the second and third amendments thereto, dated December 22, 1986, and December 23, 1987, respectively | 10.4 to APS's 1988 Form 10-K Report, File No. 1-4473 | 3/8/1989 |
| 10.2.1a[b] | Pinnacle West APS | Third Amendment to the Arizona Public Service Company Deferred Compensation Plan, effective as of January 1, 1993 | 10.3A to APS's 1993 Form 10-K Report, File No. 1-4473 | 3/30/1994 |
| 10.2.1b[b] | Pinnacle West APS | Fourth Amendment to the Arizona Public Service Company Deferred Compensation Plan effective as of May 1, 1993 | 10.2 to APS's September 30, 1994 Form 10-Q Report, File No. 1-4473 | 11/10/1994 |
| 10.2.1c[b] | Pinnacle West | Fifth Amendment to the Arizona Public Service Company Deferred Compensation Plan effective | 10.3A to APS's 1996 Form 10-K Report, File | 3/28/1997 |

| | | | | |
|---|---|---|---|---|
| | APS | January 1, 1997 | No. 1-4473 | |
| 10.2.1d[b] | Pinnacle West APS | Sixth Amendment to the Arizona Public Service Company Deferred Compensation Plan effective January 1, 2001 | 10.8A to Pinnacle West's 2000 Form 10-K Report, File No. 1-8962 | 3/14/2001 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.2.2[b] | Pinnacle West APS | Arizona Public Service Company Directors' Deferred Compensation Plan, as restated, effective January 1, 1986 | 10.1 to APS's June 30, 1986 Form 10-Q Report, File No. 1-4473 | 8/13/1986 |
| 10.2.2a[b] | Pinnacle West APS | Second Amendment to the Arizona Public Service Company Directors' Deferred Compensation Plan, effective as of January 1, 1993 | 10.2A to APS's 1993 Form 10-K Report, File No. 1-4473 | 3/30/1994 |
| 10.2.2b[b] | Pinnacle West APS | Third Amendment to the Arizona Public Service Company Directors' Deferred Compensation Plan, effective as of May 1, 1993 | 10.1 to APS's September 30, 1994 Form 10-Q Report, File No. 1-4473 | 11/10/1994 |
| 10.2.2c[b] | Pinnacle West APS | Fourth Amendment to the Arizona Public Service Company Directors Deferred Compensation Plan, effective as of January 1, 1999 | 10.8A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962 | 3/30/2000 |
| 10.2.3[b] | Pinnacle West APS | Trust for the Pinnacle West Capital Corporation, Arizona Public Service Company and SunCor Development Company Deferred Compensation Plans dated August 1, 1996 | 10.14A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962 | 3/30/2000 |
| 10.2.3a[b] | Pinnacle West APS | First Amendment dated December 7, 1999 to the Trust for the Pinnacle West Capital Corporation, Arizona Public Service Company and SunCor Development Company Deferred Compensation Plans | 10.15A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962 | 3/30/2000 |
| 10.2.4[b] | Pinnacle West APS | Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan as amended and restated effective January 1, 1996 | 10.10A to APS's 1995 Form 10-K Report, File No. 1-4473 | 3/29/1996 |
| 10.2.4a[b] | Pinnacle West APS | First Amendment effective as of January 1, 1999, to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan | 10.7A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962 | 3/30/2000 |
| 10.2.4b[b] | Pinnacle West APS | Second Amendment effective January 1, 2000 to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan | 10.10A to Pinnacle West's 1999 Form 10-K Report, File No. 1-8962 | 3/30/2000 |
| 10.2.4c[b] | Pinnacle West APS | Third Amendment to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado | 10.3 to Pinnacle West's March 31, 2003 Form 10-Q Report, File No. 1-8962 | 5/15/2003 |

Investment Company Deferred Compensation Plan,
effective as of January 1, 2002

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.2.4d[b] | Pinnacle West APS | Fourth Amendment to the Pinnacle West Capital Corporation, Arizona Public Service Company, SunCor Development Company and El Dorado Investment Company Deferred Compensation Plan, effective January 1, 2003 | 10.64b to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/13/2006 |
| 10.2.5[b] | Pinnacle West APS | Deferred Compensation Plan of 2005 for Employees of Pinnacle West Capital Corporation and Affiliates (as amended and restated effective January 1, 2016) | 10.2.5 to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/19/2016 |
| 10.3.1[b] | Pinnacle West APS | Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan, amended and restated as of January 1, 2003 | 10.7A to Pinnacle West's 2003 Form 10-K Report, File No. 1-8962 | 3/15/2004 |
| 10.3.1a[b] | Pinnacle West APS | Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan, as amended and restated, dated December 18, 2003 | 10.48b to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/13/2006 |
| 10.3.2[b] | Pinnacle West APS | Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016) | 10.3.2 to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/19/2016 |
| 10.3.2a[b] | Pinnacle West APS | First Amendment to the Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016) | 10.3.2a to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/24/2017 |
| 10.3.2b[b] | Pinnacle West APS | Second Amendment to the Pinnacle West Capital Corporation Supplemental Excess Benefit Retirement Plan of 2005 (as amended and restated effective January 1, 2016) | 10.3.2b to Pinnacle West/APS 2017 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/23/2018 |
| 10.4.1[b] | Pinnacle West APS | Letter Agreement dated June 17, 2008 between Pinnacle West/APS and James R. Hatfield | 10.1 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/7/2008 |
| 10.4.2[b] | APS | Retention Agreement dated December 19, 2008 between APS and Robert Bement | | |
| 10.4.3[b] | APS | Discretionary Credit Award Agreement dated October 20, 2014 between APS and Robert Bement | | |
| 10.5.1[bd] | Pinnacle West APS | Key Executive Employment and Severance Agreement between Pinnacle West and certain executive officers of Pinnacle West and its subsidiaries | 10.77bd to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/13/2006 |

| | | | | |
|---|---|---|---|---|
| 10.5.1a[bd] | Pinnacle West APS | Form of Amended and Restated Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries | 10.4 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 11/6/2007 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.5.2[bd] | Pinnacle West APS | Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries | 10.3 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 11/6/2007 |
| 10.5.3[bd] | Pinnacle West APS | Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries | 10.5.3 to Pinnacle West/APS 2009 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/19/2010 |
| 10.5.4[bd] | Pinnacle West APS | Form of Key Executive Employment and Severance Agreement between Pinnacle West and certain officers of Pinnacle West and its subsidiaries | 10.5.4 to Pinnacle West/APS 2012 Form 10-K, File Nos. 1-8962 and 1-4473 | 2/22/2013 |
| 10.6.1[b] | Pinnacle West | Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | Appendix B to the Proxy Statement for Pinnacle West's 2007 Annual Meeting of Shareholders, File No. 1-8962 | 4/20/2007 |
| 10.6.1a[b] | Pinnacle West | First Amendment to the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.2 to Pinnacle West/APS April 18, 2007 Form 8-K Report, File No. 1-8962 | 4/20/2007 |
| 10.6.1b[bd] | Pinnacle West APS | Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.3 to Pinnacle West/APS March 31, 2009 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/5/2009 |
| 10.6.1c[bd] | Pinnacle West | Form of Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.1 to Pinnacle West/APS June 30, 2010 Form 10-Q Report, File No. 1-8962 | 8/3/2010 |
| 10.6.1d[bd] | Pinnacle West | Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.2 to Pinnacle West/APS June 30, 2010 Form 10-Q Report, File No. 1-8962 | 8/3/2010 |
| 10.6.1e[bd] | Pinnacle West | Form of Performance Share Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.4 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962 | 4/29/2011 |
| 10.6.1f[bd] | Pinnacle West | Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan | 10.5 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962 | 4/29/2011 |
| 10.6.1g[bd] | | | | 4/29/2011 |

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|---|---|---|---|---|
| | Pinnacle West | Form of Restricted Stock Unit Agreement under the Pinnacle West Capital Corporation 2007 Long-Term Incentive Plan (Supplemental 2010 Award) | 10.6 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File No. 1-8962 | |
| 10.6.2[b] | Pinnacle West | Description of Annual Stock Grants to Non-Employee Directors | 10.1 to Pinnacle West/APS September 30, 2007 Form 10-Q Report, File No. 1-8962 | 11/6/2007 |
| 10.6.3[b] | Pinnacle West | Description of Annual Stock Grants to Non-Employee Directors | 10.2 to Pinnacle West/APS June 30, 2008 Form 10-Q Report, File No. 1-8962 | 8/7/2008 |
| 10.6.4[bd] | Pinnacle West APS | Summary of 2019 Variable Incentive Plan and Officer Variable Incentive Plan | | |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.6.5 | Pinnacle West | Description of Restricted Stock Unit Grant to Donald E. Brandt | Pinnacle West/APS December 24, 2012 Form 8-K Report, File No. 1-8962 | 12/26/2012 |
| 10.6.6[b] | Pinnacle West APS | Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | Appendix A to the Proxy Statement for Pinnacle West's 2012 Annual Meeting of Shareholders, File No. 1-8962 | 3/29/2012 |
| 10.6.6a[bd] | Pinnacle West | Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.1 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/3/2012 |
| 10.6.6b[bd] | Pinnacle West | Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.2 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/3/2012 |
| 10.6.6c[bd] | Pinnacle West | Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.6.8c to Pinnacle West/APS 2013 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/21/2014 |
| 10.6.6d[bd] | Pinnacle West | Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.6.8d to Pinnacle West/APS 2013 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/21/2014 |
| 10.6.6e[bd] | Pinnacle West | Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.6.6e to Pinnacle West/APS 2015 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/19/2016 |
| 10.6.6f[bd] | Pinnacle West | Form of Restricted Stock Unit Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.6.6f to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/24/2017 |
| 10.6.6g[bd] | Pinnacle West | Form of Performance Share Award Agreement under the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | 10.6.6g to Pinnacle West/APS 2016 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/24/2017 |
| 10.6.6h[bd] | Pinnacle West | Master Amendment to Performance Share Agreements | 10.3 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/3/2012 |
| 10.6.6i[bd] | Pinnacle West | Master Amendment to Restricted Stock Unit Agreements | 10.4 to Pinnacle West/APS March 31, 2012 Form 10-Q Report, File Nos. 1-8962 | 5/3/2012 |

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|---|---|---|---|---|
| | | | and 1-4473 | |
| 10.6.6j[bd] | Pinnacle West | Performance Cash Award Agreement, dated May 10, 2017, between Pinnacle West and Donald E. Brandt | 10.1 to Pinnacle West/APS June 30, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/2/2017 |
| 10.6.6k[bd] | Pinnacle West | First Amendment to the Pinnacle West Capital Corporation 2012 Long-Term Incentive Plan | Appendix A to the Proxy Statement for Pinnacle West's 2017 Annual Meeting of Shareholders, File No. 1-8962 | 3/31/2017 |
| 10.7.1 | Pinnacle West APS | Indenture of Lease with Navajo Tribe of Indians, Four Corners Plant | 5.01 to APS's Form S-7 Registration Statement, File No. 2-59644 | 9/1/1977 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.7.1a | Pinnacle West APS | Supplemental and Additional Indenture of Lease, including amendments and supplements to original lease with Navajo Tribe of Indians, Four Corners Plant | 5.02 to APS's Form S-7 Registration Statement, File No. 2-59644 | 9/1/1977 |
| 10.7.1b | Pinnacle West APS | Amendment and Supplement No. 1 to Supplemental and Additional Indenture of Lease Four Corners, dated April 25, 1985 | 10.36 to Pinnacle West's Registration Statement on Form 8-B Report, File No. 1-89 | 7/25/1985 |
| 10.7.1c | Pinnacle West APS | Amendment and Supplement No. 2 to Supplemental and Additional Indenture of Lease with the Navajo Nation dated March 7, 2011 | 10.1 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 4/29/2011 |
| 10.7.1d | Pinnacle West APS | Amendment and Supplement No. 3 to Supplemental and Additional Indenture of Lease with the Navajo Nation dated March 7, 2011 | 10.2 to Pinnacle West/APS March 31, 2011 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 4/29/2011 |
| 10.7.2 | Pinnacle West APS | Application and Grant of multi-party rights-of-way and easements, Four Corners Plant Site | 5.04 to APS's Form S-7 Registration Statement, File No. 2-59644 | 9/1/1977 |
| 10.7.2a | Pinnacle West APS | Application and Amendment No. 1 to Grant of multi-party rights-of-way and easements, Four Corners Site dated April 25, 1985 | 10.37 to Pinnacle West's Registration Statement on Form 8-B, File No. 1-8962 | 7/25/1985 |
| 10.7.3 | Pinnacle West APS | Application and Grant of APS rights- of-way and easements, Four Corners Site | 5.05 to APS's Form S-7 Registration Statement, File No. 2-59644 | 9/1/1977 |
| 10.7.3a | Pinnacle West APS | Application and Amendment No. 1 to Grant of APS rights-of-way and easements, Four Corners Site dated April 25, 1985 | 10.38 to Pinnacle West's Registration Statement on Form 8-B, File No. 1-8962 | 7/25/1985 |
| 10.7.4 | Pinnacle West APS | Four Corners Project Co-Tenancy Agreement, conformed copy up through and including Amendment No. 11, dated June 30, 2018, among APS, Public Service Company of New Mexico, SRP, Tucson Electric Power Company and Navajo Transitional Energy Company, LLC | 10.7.4c to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |
| 10.8.1 | Pinnacle West APS | Indenture of Lease, Navajo Units 1, 2, and 3 | 5(g) to APS's Form S-7 Registration Statement, File No. 2-36505 | 3/23/1970 |
| 10.8.2 | Pinnacle West | Application of Grant of rights-of-way and easements, Navajo Plant | 5(h) to APS Form S-7 Registration Statement, File | 3/23/1970 |

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|---|---|---|---|---|
| | APS | | No. 2-36505 | |
| 10.8.3 | Pinnacle West APS | Water Service Contract Assignment with the United States Department of Interior, Bureau of Reclamation, Navajo Plant | 5(l) to APS's Form S-7 Registration Statement, File No. 2-394442 | 3/16/1971 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.8.4 | Pinnacle West APS | Navajo Project Co-Tenancy Agreement dated as of March 23, 1976, and Supplement No. 1 thereto dated as of October 18, 1976, Amendment No. 1 dated as of July 5, 1988, and Amendment No. 2 dated as of June 14, 1996; Amendment No. 3 dated as of February 11, 1997; Amendment No. 4 dated as of January 21, 1997; Amendment No. 5 dated as of January 23, 1998; Amendment No. 6 dated as of July 31, 1998 | 10.107 to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/13/2006 |
| 10.8.5 | Pinnacle West APS | Navajo Project Participation Agreement dated as of September 30, 1969, and Amendment and Supplement No. 1 dated as of January 16, 1970, and Coordinating Committee Agreement No. 1 dated as of September 30, 1971 | 10.108 to Pinnacle West/APS 2005 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/13/2006 |
| 10.9.1 | Pinnacle West APS | ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles, and amendments 1-12 thereto | 10. 1 to APS's 1988 Form 10-K Report, File No. 1-4473 | 3/8/1989 |
| 10.9.1a | Pinnacle West APS | Amendment No. 13, dated as of April 22, 1991, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles | 10.1 to APS's March 31, 1991 Form 10-Q Report, File No. 1-4473 | 5/15/1991 |
| 10.9.1b | Pinnacle West APS | Amendment No. 14 to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles | 99.1 to Pinnacle West's June 30, 2000 Form 10-Q Report, File No. 1-8962 | 8/14/2000 |
| 10.9.1c | Pinnacle West APS | Amendment No. 15, dated November 29, 2010, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles | 10.9.1c to Pinnacle West/APS 2010 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/18/2011 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.9.1d | Pinnacle West APS | Amendment No. 16, dated April 28, 2014, to ANPP Participation Agreement, dated August 23, 1973, among APS, SRP, SCE, Public Service Company of New Mexico, El Paso, Southern California Public Power Authority, and Department of Water and Power of the City of Los Angeles | 10.2 to Pinnacle West/APS March 31, 2014 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/2/2014 |
| 10.10.1 | Pinnacle West APS | Asset Purchase and Power Exchange Agreement dated September 21, 1990 between APS and PacifiCorp, as amended as of October 11, 1990 and as of July 18, 1991 | 10.1 to APS's June 30, 1991 Form 10-Q Report, File No. 1-4473 | 8/8/1991 |
| 10.10.2 | Pinnacle West APS | Long-Term Power Transaction Agreement dated September 21, 1990 between APS and PacifiCorp, as amended as of October 11, 1990, and as of July 8, 1991 | 10.2 to APS's June 30, 1991 Form 10-Q Report, File No. 1-4473 | 8/8/1991 |
| 10.10.2a | Pinnacle West APS | Amendment No. 1 dated April 5, 1995 to the Long-Term Power Transaction Agreement and Asset Purchase and Power Exchange Agreement between PacifiCorp and APS | 10.3 to APS's 1995 Form 10-K Report, File No. 1-4473 | 3/29/1996 |
| 10.10.3 | Pinnacle West APS | Restated Transmission Agreement between PacifiCorp and APS dated April 5, 1995 | 10.4 to APS's 1995 Form 10-K Report, File No. 1-4473 | 3/29/1996 |
| 10.10.4 | Pinnacle West APS | Contract among PacifiCorp, APS and DOE Western Area Power Administration, Salt Lake Area Integrated Projects for Firm Transmission Service dated May 5, 1995 | 10.5 to APS's 1995 Form 10-K Report, File No. 1-4473 | 3/29/1996 |
| 10.10.5 | Pinnacle West APS | Reciprocal Transmission Service Agreement between APS and PacifiCorp dated as of March 2, 1994 | 10.6 to APS's 1995 Form 10-K Report, File No. 1-4473 | 3/29/1996 |
| 10.11.1 | Pinnacle West | Term Loan Agreement dated as of December 21, 2018 among Pinnacle West, as Borrower, KeyBank National Association, as Agent, PNC Bank, National Association and Wells Fargo Bank, National Association, as Co-Syndication Agents and such institutions compromising the lenders party thereto | | |
| 10.11.2 | Pinnacle West | Five-Year Credit Agreement dated as of July 12, 2018, among Pinnacle West, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto | 10.3 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.11.3 | Pinnacle West | 364-day Credit Agreement dated as of June 28, 2018, among Pinnacle West, as Borrower, MUFG Bank, Ltd., as Agent and Issuing Bank, JPMorgan Chase Bank, N.A. and Bank of America, N.A., as Co-Syndication Agent | 10.1 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |
| 10.11.4 | Pinnacle West APS | Five-Year Credit Agreement dated as of June 29, 2017 among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto | 10.2 to Pinnacle West/APS June 30, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2017 |
| 10.11.4a | Pinnacle West APS | Amendment No. 1, dated July 13, 2018, to Five-Year Credit Agreement dated as of June 29, 2017, among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto | 10.11.4a to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |
| 10.11.5 | Pinnacle West APS | Five-Year Credit Agreement dated as of July 12, 2018 among APS, as Borrower, Barclays Bank PLC, as Agent and Issuing Bank, and the lenders and other parties thereto | 10.4 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |
| 10.12.1[c] | Pinnacle West APS | Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee | 4.3 to APS's Form 18 Registration Statement, File No. 33-9480 | 10/24/1986 |
| 10.12.1a[c] | Pinnacle West APS | Amendment No. 1, dated as of November 1, 1986, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee | 10.5 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1 on December 3, 1986 Form 8, File No. 1-4473 | 12/4/1986 |
| 10.12.1b[c] | Pinnacle West APS | Amendment No. 2 dated as of June 1, 1987 to Facility Lease dated as of August 1, 1986 between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee | 10.3 to APS's 1988 Form 10-K Report, File No. 1-4473 | 3/8/1989 |
| 10.12.1c[c] | Pinnacle West APS | Amendment No. 3, dated as of March 17, 1993, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, | 10.3 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |

successor to State Street Bank and Trust
Company, as successor to The First National
Bank of Boston, as Lessor, and APS, as Lessee

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.12.1d[c] | Pinnacle West APS | Amendment No. 4, dated as of September 30, 2015, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee under a Trust Agreement with Emerson Finance LLC, as Lessor, and APS, as Lessee | 10.2 to Pinnacle West/APS September 30, 2015 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 10/30/2015 |
| 10.12.1e[c] | Pinnacle West APS | Amendment No. 3, dated as of September 30, 2015, to Facility Lease, dated as of August 1, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee under a Trust Agreement with Security Pacific Capital Leasing Corporation, as Lessor, and APS, as Lessee | 10.3 to Pinnacle West/APS September 30, 2015 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 10/30/2015 |
| 10.12.2 | Pinnacle West APS | Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its capacity as Owner Trustee, as Lessor, and APS, as Lessee | 10.1 to APS's November 18, 1986 Form 8-K Report, File No. 1-4473 | 1/20/1987 |
| 10.12.2a | Pinnacle West APS | Amendment No. 1, dated as of August 1, 1987, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee | 4.13 to APS's Form 18 Registration Statement No. 33-9480 by means of August 1, 1987 Form 8-K Report, File No. 1-4473 | 8/24/1987 |
| 10.12.2b | Pinnacle West APS | Amendment No. 2, dated as of March 17, 1993, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Lessor, and APS, as Lessee | 10.4 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 10.12.2c | Pinnacle West APS | Amendment No. 3, dated July 10, 2014, to Facility Lease, dated as of December 15, 1986, between U.S. Bank National Association, successor to State Street Bank and Trust Company, as successor to the First National Bank of Boston, as Lessor, and APS, as Lessee | 10.2 to Pinnacle West/APS June 30, 2014 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 7/31/2014 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.13.1 | Pinnacle West APS | Agreement between Pinnacle West Energy Corporation and APS for Transportation and Treatment of Effluent by and between Pinnacle West Energy Corporation and APS dated as of the 10th day of April, 2001 | 10.102 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/16/2005 |
| 10.13.2 | Pinnacle West APS | Agreement for the Transfer and Use of Wastewater and Effluent by and between APS, SRP and PWE dated June 1, 2001 | 10.103 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/16/2005 |
| 10.13.3 | Pinnacle West APS | Agreement for the Sale and Purchase of Wastewater Effluent dated November 13, 2000, by and between the City of Tolleson, Arizona, APS and SRP | 10.104 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/16/2005 |
| 10.13.4 | Pinnacle West APS | Operating Agreement for the Co-Ownership of Wastewater Effluent dated November 16, 2000 by and between APS and SRP | 10.105 to Pinnacle West/APS 2004 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 3/16/2005 |
| 10.13.5 | Pinnacle West APS | Municipal Effluent Purchase and Sale Agreement dated April 29, 2010, by and between City of Phoenix, City of Mesa, City of Tempe, City of Scottsdale, City of Glendale, APS and SRP | 10.1 to Pinnacle West/APS March 31, 2010 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/6/2010 |
| 10.14.1 | Pinnacle West APS | Contract, dated July 21, 1984, with DOE providing for the disposal of nuclear fuel and/or high-level radioactive waste, ANPP | 10.31 to Pinnacle West's Form S-14 Registration Statement, File No. 2-96386 | 3/13/1985 |
| 10.15.1 | Pinnacle West APS | Territorial Agreement between APS and SRP | 10.1 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473 | 5/15/1998 |
| 10.15.2 | Pinnacle West APS | Power Coordination Agreement between APS and SRP | 10.2 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473 | 5/15/1998 |
| 10.15.3 | Pinnacle West APS | Memorandum of Agreement between APS and SRP | 10.3 to APS's March 31, 1998 Form 10-Q Report, File No. 1-4473 | 5/15/1998 |
| 10.15.3a | Pinnacle West APS | Addendum to Memorandum of Agreement between APS and SRP dated as of May 19, 1998 | 10.2 to APS's May 19, 1998 Form 8-K Report, File No. 1-4473 | 6/26/1998 |
| 10.16 | Pinnacle West APS | Purchase and Sale Agreement dated November 8, 2010 by and between SCE and APS | 10.1 to Pinnacle West/APS November 8, 2010 Form 8-K Report, File Nos. 1-8962 and | 11/8/2010 |

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|---|---|---|---|---|
| | | | 1-4473 | |
| 10.17 | Pinnacle West APS | Proposed Settlement Agreement dated January 6, 2012 by and among APS and certain parties to its retail rate case (approved by ACC Order No. 73183) | 10.17 to Pinnacle West/APS 2011 Form 10-K Report, File Nos. 1-8962 and 1-4473 | 2/24/2012 |
| 10.18 | Pinnacle West APS | Proposed Settlement Agreement dated March 27, 2017 by and among APS and certain parties to its retail rate case (approved by ACC Order No. 76295) | 10.1 to Pinnacle West/APS March 31, 2017 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 5/2/2017 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 10.19 | Pinnacle West | Purchase and Sale Agreement, dated June 29, 2018, by and between Navajo Transitional Energy Company, LLC and 4CA | 10.2 to Pinnacle West/APS June 30, 2018 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/3/2018 |
| 21.1 | Pinnacle West | Subsidiaries of Pinnacle West | | |
| 23.1 | Pinnacle West | Consent of Deloitte & Touche LLP | | |
| 23.2 | APS | Consent of Deloitte & Touche LLP | | |
| 31.1 | Pinnacle West | Certificate of Donald E. Brandt, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended | | |
| 31.2 | Pinnacle West | Certificate of James R. Hatfield, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended | | |
| 31.3 | APS | Certificate of Donald E. Brandt, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended | | |
| 31.4 | APS | Certificate of James R. Hatfield, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended | | |
| 32.1[e] | Pinnacle West | Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | |
| 32.2[e] | APS | Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | |
| 99.1 | Pinnacle West APS | Collateral Trust Indenture among PVGS II Funding Corp., Inc., APS and Chemical Bank, as Trustee | 4.2 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.1a | Pinnacle West APS | Supplemental Indenture to Collateral Trust Indenture among PVGS II Funding Corp., Inc., APS and Chemical Bank, as Trustee | 4.3 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.2[c] | | | | 11/9/1992 |

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|---|---|---|
| Pinnacle West APS | Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., Bank of America National Trust and Savings Association, State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein | 28.1 to APS's September 30, 1992 Form 10-Q Report, File No. 1-4473 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 99.2a[c] | Pinnacle West APS | Amendment No. 1 dated as of November 1, 1986, to Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., Bank of America National Trust and Savings Association, State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein | 10.8 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1, on December 3, 1986 Form 8, File No. 1-4473 | 12/4/1986 |
| 99.2b[c] | Pinnacle West APS | Amendment No. 2, dated as of March 17, 1993, to Participation Agreement, dated as of August 1, 1986, among PVGS Funding Corp., Inc., PVGS II Funding Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Equity Participant named therein | 28.4 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.3[c] | Pinnacle West APS | Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee | 4.5 to APS's Form 18 Registration Statement, File No. 33-9480 | 10/24/1986 |
| 99.3a[c] | Pinnacle West APS | Supplemental Indenture No. 1, dated as of November 1, 1986 to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee | 10.6 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. 1 on December 3, 1986 Form 8, File No. 1-4473 | 12/4/1986 |
| 99.3b[c] | Pinnacle West APS | Supplemental Indenture No. 2 to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of August 1, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Lease Indenture Trustee | 4.4 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.4[c] | Pinnacle West APS | Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee | 28.3 to APS's Form 18 Registration Statement, File No. 33-9480 | 10/24/1986 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 99.4a[c] | Pinnacle West APS | Amendment No. 1, dated as of November 1, 1986, to Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee | 10.10 to APS's September 30, 1986 Form 10-Q Report by means of Amendment No. l on December 3, 1986 Form 8, File No. 1-4473 | 12/4/1986 |
| 99.4b[c] | Pinnacle West APS | Amendment No. 2, dated as of March 17, 1993, to Assignment, Assumption and Further Agreement, dated as of August 1, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee | 28.6 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.5 | Pinnacle West APS | Participation Agreement, dated as of December 15, 1986, among PVGS Funding Report Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee under a Trust Indenture, APS, and the Owner Participant named therein | 28.2 to APS's September 30, 1992 Form 10-Q Report, File No. 1-4473 | 11/9/1992 |
| 99.5a | Pinnacle West APS | Amendment No. 1, dated as of August 1, 1987, to Participation Agreement, dated as of December 15, 1986, among PVGS Funding Corp., Inc. as Funding Corporation, State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, Chemical Bank, as Indenture Trustee, APS, and the Owner Participant named therein | 28.20 to APS's Form 18 Registration Statement No. 33-9480 by means of a November 6, 1986 Form 8-K Report, File No. 1-4473 | 8/10/1987 |
| 99.5b | Pinnacle West APS | Amendment No. 2, dated as of March 17, 1993, to Participation Agreement, dated as of December 15, 1986, among PVGS Funding Corp., Inc., PVGS II Funding Corp., Inc., State Street Bank and Trust Company, as successor to The First National Bank of Boston, in its individual capacity and as Owner Trustee, Chemical Bank, in its individual capacity and as Indenture Trustee, APS, and the Owner Participant named therein | 28.5 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.6 | Pinnacle West APS | Trust Indenture, Mortgage Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee | 10.2 to APS's November 18, 1986 Form 10-K Report, File No. 1-4473 | 1/20/1987 |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: a | Date Filed |
|---|---|---|---|---|
| 99.6a | Pinnacle West APS | Supplemental Indenture No. 1, dated as of August 1, 1987, to Trust Indenture, Mortgage, Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Indenture Trustee | 4.13 to APS's Form 18 Registration Statement No. 33-9480 by means of August 1, 1987 Form 8-K Report, File No. 1-4473 | 8/24/1987 |
| 99.6b | Pinnacle West APS | Supplemental Indenture No. 2 to Trust Indenture Mortgage, Security Agreement and Assignment of Facility Lease, dated as of December 15, 1986, between State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee, and Chemical Bank, as Lease Indenture Trustee | 4.5 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.7 | Pinnacle West APS | Assignment, Assumption and Further Agreement, dated as of December 15, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee | 10.5 to APS's November 18, 1986 Form 8-K Report, File No. 1-4473 | 1/20/1987 |
| 99.7a | Pinnacle West APS | Amendment No. 1, dated as of March 17, 1993, to Assignment, Assumption and Further Agreement, dated as of December 15, 1986, between APS and State Street Bank and Trust Company, as successor to The First National Bank of Boston, as Owner Trustee | 28.7 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.8[c] | Pinnacle West APS | Indemnity Agreement dated as of March 17, 1993 by APS | 28.3 to APS's 1992 Form 10-K Report, File No. 1-4473 | 3/30/1993 |
| 99.9 | Pinnacle West APS | Extension Letter, dated as of August 13, 1987, from the signatories of the Participation Agreement to Chemical Bank | 28.20 to APS's Form 18 Registration Statement No. 33-9480 by means of a November 6, 1986 Form 8-K Report, File No. 1-4473 | 8/10/1987 |
| 99.10 | Pinnacle West APS | ACC Order, Decision No. 61969, dated September 29, 1999, including the Retail Electric Competition Rules | 10.2 to APS's September 30, 1999 Form 10-Q Report, File No. 1-4473 | 11/15/1999 |
| 99.11 | Pinnacle West | Purchase Agreement by and among Pinnacle West Energy Corporation and GenWest, L.L.C. and Nevada Power Company, dated June 21, 2005 | 99.5 to Pinnacle West/APS June 30, 2005 Form 10-Q Report, File Nos. 1-8962 and 1-4473 | 8/9/2005 |

| | | |
|---|---|---|
| 101.SCH | Pinnacle West APS | XBRL Taxonomy Extension Schema Document |
| 101.CAL | Pinnacle West APS | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.LAB | Pinnacle West APS | XBRL Taxonomy Extension Label Linkbase Document |

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| Exhibit No. | Registrant(s) | Description | Previously Filed as Exhibit: [a] | Date Filed |
|---|---|---|---|---|
| 101.PRE | Pinnacle West APS | XBRL Taxonomy Extension Presentation Linkbase Document | | |
| 101.DEF | Pinnacle West APS | XBRL Taxonomy Definition Linkbase Document | | |

[a]Reports filed under File No. 1-4473 and 1-8962 were filed in the office of the Securities and Exchange Commission located in Washington, D.C.

[b]Management contract or compensatory plan or arrangement to be filed as an exhibit pursuant to Item 15(b) of Form 10-K.

[c]An additional document, substantially identical in all material respects to this Exhibit, has been entered into, relating to an additional Equity Participant. Although such additional document may differ in other respects (such as dollar amounts, percentages, tax indemnity matters, and dates of execution), there are no material details in which such document differs from this Exhibit.

[d]Additional agreements, substantially identical in all material respects to this Exhibit have been entered into with additional persons. Although such additional documents may differ in other respects (such as dollar amounts and dates of execution), there are no material details in which such agreements differ from this Exhibit.

[e]Furnished herewith as an Exhibit.

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

| | |
|---|---|
| | PINNACLE WEST CAPITAL CORPORATION<br>(Registrant) |
| Date: February 22, 2019 | /s/ Donald E. Brandt<br>(Donald E. Brandt, Chairman of the Board of Directors, President and Chief Executive Officer) |

## Power of Attorney

We, the undersigned directors and executive officers of Pinnacle West Capital Corporation, hereby severally appoint James R. Hatfield and Robert E. Smith, and each of them, our true and lawful attorneys with full power to them and each of them to sign for us, and in our names in the capacities indicated below, any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature | Title | Date |
|---|---|---|
| /s/ Donald E. Brandt<br>(Donald E. Brandt, Chairman of the Board of Directors, President and Chief Executive Officer) | Principal Executive Officer and Director | February 22, 2019 |
| /s/ James R. Hatfield<br>(James R. Hatfield, Executive Vice President and Chief Financial Officer) | Principal Financial Officer | February 22, 2019 |
| /s/ Denise R. Danner<br>(Denise R. Danner, Vice President, Controller and Chief Accounting Officer) | Principal Accounting Officer | February 22, 2019 |

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| | | |
|---|---|---|
| /s/ Denis A. Cortese, M.D.<br>(Denis A. Cortese, M.D.) | Director | February 22, 2019 |
| /s/ Richard P. Fox<br>(Richard P. Fox) | Director | February 22, 2019 |
| /s/ Michael L. Gallagher<br>(Michael L. Gallagher) | Director | February 22, 2019 |
| /s/ Dale E. Klein, Ph.D.<br>(Dale E. Klein, Ph.D.) | Director | February 22, 2019 |
| /s/ Humberto S. Lopez<br>(Humberto S. Lopez) | Director | February 22, 2019 |
| /s/ Kathryn L. Munro<br>(Kathryn L. Munro) | Director | February 22, 2019 |
| /s/ Bruce J. Nordstrom<br>(Bruce J. Nordstrom) | Director | February 22, 2019 |
| /s/ Paula J. Sims<br>(Paula J. Sims) | Director | February 22, 2019 |
| /s/ James E. Trevathan<br>(James E. Trevathan) | Director | February 22, 2019 |
| /s/ David P. Wagener<br>(David P. Wagener) | Director | February 22, 2019 |

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

| | |
|---|---|
| | ARIZONA PUBLIC SERVICE COMPANY<br>(Registrant) |
| Date: February 22, 2019 | /s/ Donald E. Brandt<br>(Donald E. Brandt, Chairman of the Board of Directors and Chief Executive Officer) |

## Power of Attorney

We, the undersigned directors and executive officers of Arizona Public Service Company, hereby severally appoint James R. Hatfield and Robert E. Smith, and each of them, our true and lawful attorneys with full power to them and each of them to sign for us, and in our names in the capacities indicated below, any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature | Title | Date |
|---|---|---|
| /s/ Donald E. Brandt<br>(Donald E. Brandt, Chairman of the Board of Directors and Chief Executive Officer) | Principal Executive Officer and Director | February 22, 2019 |
| /s/ James R. Hatfield<br>(James R. Hatfield, Executive Vice President and Chief Financial Officer) | Principal Financial Officer | February 22, 2019 |
| /s/ Denise R. Danner<br>(Denise R. Danner, Vice President, Controller and Chief Accounting Officer) | Principal Accounting Officer | February 22, 2019 |

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| | | |
|---|---|---|
| /s/ Denis A. Cortese, M.D.<br>(Denis A. Cortese, M.D.) | Director | February 22, 2019 |
| /s/ Richard P. Fox<br>(Richard P. Fox) | Director | February 22, 2019 |
| /s/ Michael L. Gallagher<br>(Michael L. Gallagher) | Director | February 22, 2019 |
| /s/ Dale E. Klein<br>(Dale E. Klein, Ph.D.) | Director | February 22, 2019 |
| /s/ Humberto S. Lopez<br>(Humberto S. Lopez) | Director | February 22, 2019 |
| /s/ Kathryn L. Munro<br>(Kathryn L. Munro) | Director | February 22, 2019 |
| /s/ Bruce J. Nordstrom<br>(Bruce J. Nordstrom) | Director | February 22, 2019 |
| /s/ Paula J. Sims<br>(Paula J. Sims) | Director | February 22, 2019 |
| /s/ James E. Trevathan<br>(James E. Trevathan) | Director | February 22, 2019 |
| /s/ David P. Wagener<br>(David P. Wagener) | Director | February 22, 2019 |