

ARIZONA PUBLIC SERVICE CO

Form 10-Q

November 08, 2006

PINNACLE WEST CAPITAL CORPORATION Number of shares of common stock, no par value,
outstanding as of November 3, 2006: 99,847,829

ARIZONA PUBLIC SERVICE COMPANY Number of shares of common stock, \$2.50 par value,
outstanding as of November 3, 2006: 71,264,947

Arizona Public Service Company meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this form with the reduced disclosure format allowed under that General Instruction.

This combined Form 10-Q is separately filed by Pinnacle West Capital Corporation and Arizona Public Service Company. Each registrant is filing on its own behalf all of the information contained in this Form 10-Q that relates to such registrant and, where required, its subsidiaries. Except as stated in the preceding sentence, neither registrant is filing any information that does not relate to such registrant, and therefore makes no representation as to any such information.

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GLOSSARY

ACC	Arizona Corporation Commission
ADEQ	Arizona Department of Environmental Quality
ALJ	Administrative Law Judge
APB	Accounting Principles Board
APS	Arizona Public Service Company, a subsidiary of the Company
APS Energy Services	APS Energy Services Company, Inc., a subsidiary of the Company
Clean Air Act	Clean Air Act, as amended
Company	Pinnacle West Capital Corporation
DOE	United States Department of Energy
EITF	FASB's Emerging Issues Task Force
El Dorado	El Dorado Investment Company, a subsidiary of the Company
EPA	United States Environmental Protection Agency
ERMC	Energy Risk Management Committee
FASB	Financial Accounting Standards Board
FERC	United States Federal Energy Regulatory Commission
FIP	Federal Implementation Plan
GAAP	accounting principles generally accepted in the United States of America
IRS	United States Internal Revenue Service
kWh	kilowatt-hour
Moody's	Moody's Investors Service
MWh	megawatt-hour, one million watts per hour
NAC	collectively, NAC Holding Inc. and NAC International Inc., subsidiaries of El Dorado that were sold in November 2004
Native Load	retail and wholesale sales supplied under traditional cost-based rate regulation
NPC	Nevada Power Company
NRC	United States Nuclear Regulatory Commission
OCI	other comprehensive income
Off-System Sales	sales of electricity from generation owned by the Company that is over and above the amount required to serve APS retail customers and traditional wholesale contracts
Palo Verde	Palo Verde Nuclear Generating Station
Pinnacle West	Pinnacle West Capital Corporation, the Company
Pinnacle West Energy	Pinnacle West Energy Corporation, a subsidiary of the Company
PRP	potentially responsible party

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PSA power supply adjustor
PWEC Dedicated Assets the following power plants, each of which was transferred by Pinnacle West Energy to APS on July 29, 2005: Redhawk Units 1 and 2, West Phoenix Units 4 and 5 and Saguaro Unit 3
Salt River Project Salt River Project Agricultural Improvement and Power District
SEC United States Securities and Exchange Commission
SFAS Statement of Financial Accounting Standards
Silverhawk Silverhawk Power Station, a 570-megawatt, natural gas-fueled, combined-cycle electric generating facility located 20 miles north of Las Vegas, Nevada
Standard & Poor s Standard & Poor s Corporation
SunCor SunCor Development Company, a subsidiary of the Company
Sundance Plant 450-megawatt generating facility located approximately 55 miles southeast of Phoenix, Arizona
Superfund Comprehensive Environmental Response, Compensation and Liability Act
Trading energy-related activities entered into with the objective of generating profits on changes in market prices
2005 Form 10-K Pinnacle West/APS Annual Report on Form 10-K for the fiscal year ended December 31, 2005
VIE variable interest entity

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(unaudited)

(dollars and shares in thousands, except per share amounts)

	Three Months Ended September 30,	
	2006	2005
OPERATING REVENUES		
Regulated electricity segment	\$ 886,979	\$ 753,428
Marketing and trading segment	84,425	107,031
Real estate segment	97,871	78,755
Other revenues	7,167	16,369
Total	1,076,442	955,583
OPERATING EXPENSES		
Regulated electricity segment fuel and purchased power	314,150	203,519
Marketing and trading segment fuel and purchased power	80,906	86,945
Operations and maintenance	164,396	158,940
Real estate segment operations	78,853	67,508
Depreciation and amortization	90,390	85,763
Taxes other than income taxes	31,697	34,325
Other expense	5,610	13,521
Regulatory disallowance		143,217
Total	766,002	793,738
OPERATING INCOME	310,440	161,845
OTHER		
Allowance for equity funds used during construction	3,178	2,852
Other income (Note 14)	18,055	8,694
Other expense (Note 14)	(3,693)	(4,915)
Total	17,540	6,631
INTEREST EXPENSE		
Interest charges	50,577	46,778
Capitalized interest	(5,612)	(3,301)
Total	44,965	43,477
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	283,015	124,999
INCOME TAXES	98,836	40,305
INCOME FROM CONTINUING OPERATIONS	184,179	84,694

INCOME (LOSS) FROM DISCONTINUED OPERATIONS			
Net of income tax expense of \$3 and \$12,407 (Note 17)		(12)	19,043
NET INCOME		\$ 184,167	\$ 103,737
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING	BASIC	99,491	98,697
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING	DILUTED	99,973	98,816
EARNINGS PER WEIGHTED AVERAGE COMMON SHARE OUTSTANDING			
Income from continuing operations	basic	\$ 1.85	\$ 0.86
Net income	basic	1.85	1.05
Income from continuing operations	diluted	1.84	0.86
Net income	diluted	1.84	1.05
DIVIDENDS DECLARED PER SHARE		\$ 0.50	\$ 0.475

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

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PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(unaudited)

(dollars and shares in thousands, except per share amounts)

	Nine Months Ended September 30,	
	2006	2005
OPERATING REVENUES		
Regulated electricity segment	\$ 2,065,823	\$ 1,749,110
Marketing and trading segment	259,352	267,460
Real estate segment	318,328	232,950
Other revenues	28,173	46,763
Total	2,671,676	2,296,283
OPERATING EXPENSES		
Regulated electricity segment fuel and purchased power	735,489	442,532
Marketing and trading segment fuel and purchased power	227,797	215,347
Operations and maintenance	511,155	467,121
Real estate segment operations	248,595	190,555
Depreciation and amortization	267,308	262,030
Taxes other than income taxes	99,970	103,528
Other expenses	22,562	39,451
Regulatory disallowance		143,217
Total	2,112,876	1,863,781
OPERATING INCOME	558,800	432,502
OTHER		
Allowance for equity funds used during construction	10,612	8,407
Other income (Note 14)	34,448	18,019
Other expense (Note 14)	(12,953)	(12,985)
Total	32,107	13,441
INTEREST EXPENSE		
Interest charges	143,985	142,820
Capitalized interest	(14,595)	(10,134)
Total	129,390	132,686
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	461,517	313,257
INCOME TAXES	154,900	113,863
INCOME FROM CONTINUING OPERATIONS	306,617	199,394
INCOME (LOSS) FROM DISCONTINUED OPERATIONS		
Net of income tax expense (benefit) of \$1,415 and \$(28,586) (Note 17)	2,159	(44,474)

NET INCOME		\$ 308,776	\$ 154,920
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING	BASIC	99,277	95,642
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING	DILUTED	99,723	95,755
EARNINGS PER WEIGHTED AVERAGE COMMON SHARE OUTSTANDING			
Income from continuing operations	basic	\$ 3.09	\$ 2.08
Net income	basic	3.11	1.62
Income from continuing operations	diluted	3.07	2.08
Net income	diluted	3.10	1.62
DIVIDENDS DECLARED PER SHARE		\$ 1.50	\$ 1.425
See Notes to Pinnacle West's Condensed Consolidated Financial Statements.			

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PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)
(dollars in thousands)

	September 30, 2006	December 31, 2005
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 128,222	\$ 154,003
Investment in debt securities	203,317	
Customer and other receivables	576,107	502,681
Allowance for doubtful accounts	(5,536)	(4,979)
Materials and supplies (at average cost)	116,867	109,736
Fossil fuel (at average cost)	21,679	23,658
Assets from risk management and trading activities (Note 10)	617,440	827,779
Assets held for sale (Note 17)	22,575	202,645
Other current assets	81,145	75,869
Total current assets	1,761,816	1,891,392
INVESTMENTS AND OTHER ASSETS		
Real estate investments net	495,965	390,702
Assets from long-term risk management and trading activities (Note 10)	216,129	597,831
Decommissioning trust accounts (Note 18)	326,318	293,943
Other assets	127,153	111,931
Total investments and other assets	1,165,565	1,394,407
PROPERTY, PLANT AND EQUIPMENT		
Plant in service and held for future use	11,077,611	10,727,695
Less accumulated depreciation and amortization	3,778,560	3,622,884
Total	7,299,051	7,104,811
Construction work in progress	349,603	327,172
Intangible assets, net of accumulated amortization	93,868	90,916
Nuclear fuel, net of accumulated amortization	64,780	54,184
Net property, plant and equipment	7,807,302	7,577,083
DEFERRED DEBITS		
Deferred fuel and purchased power regulatory asset (Note 5)	209,017	172,756
Other regulatory assets	188,368	151,123
Other deferred debits	125,131	135,884

Total deferred debits	522,516	459,763
TOTAL ASSETS	\$ 11,257,199	\$ 11,322,645

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

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PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)
(dollars in thousands)

	September 30, 2006	December 31, 2005
LIABILITIES AND COMMON STOCK EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 315,027	\$ 377,107
Accrued taxes	416,401	289,235
Accrued interest	43,839	31,774
Short-term borrowings	57,400	15,673
Current maturities of long-term debt	85,440	384,947
Customer deposits	69,088	60,509
Deferred income taxes	12,389	94,710
Liabilities from risk management and trading activities (Note 10)	523,797	720,693
Other current liabilities (Note 10)	157,889	297,425
Total current liabilities	1,681,270	2,272,073
LONG-TERM DEBT LESS CURRENT MATURITIES	3,237,423	2,608,455
DEFERRED CREDITS AND OTHER		
Deferred income taxes	1,174,003	1,225,253
Regulatory liabilities	588,957	592,494
Liability for asset retirements	282,060	269,011
Pension liability	267,744	264,476
Liabilities from long-term risk management and trading activities (Note 10)	194,196	256,413
Unamortized gain - sale of utility plant	42,325	45,757
Other	394,149	363,749
Total deferred credits and other	2,943,434	3,017,153
COMMITMENTS AND CONTINGENCIES (Notes 5, 12, 13 and 15)		
COMMON STOCK EQUITY		
Common stock, no par value	2,094,942	2,067,377
Treasury stock	(406)	(1,245)
Total common stock	2,094,536	2,066,132
Accumulated other comprehensive income (loss) (Note 11):		
Minimum pension liability adjustment	(97,277)	(97,277)
Derivative instruments	44,200	262,397

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Total accumulated other comprehensive income (loss)	(53,077)	165,120
Retained earnings	1,353,613	1,193,712
Total common stock equity	3,395,072	3,424,964
TOTAL LIABILITIES AND COMMON STOCK EQUITY	\$ 11,257,199	\$ 11,322,645

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

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PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(dollars in thousands)

	Nine Months Ended September 30,	
	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$ 308,776	\$ 154,920
Adjustments to reconcile net income to net cash provided by operating activities:		
Silverhawk impairment loss		91,057
Regulatory disallowance		143,217
Depreciation and amortization including nuclear fuel	288,065	292,190
Deferred fuel and purchased power	(231,388)	(142,806)
Deferred fuel and purchased power amortization	195,127	
Allowance for equity funds used during construction	(10,612)	(8,407)
Deferred income taxes	3,598	(51,045)
Change in mark-to-market valuations	16,974	(29,785)
Changes in current assets and liabilities:		
Customer and other receivables	(72,154)	(126,450)
Materials, supplies and fossil fuel	135	(15,581)
Other current assets	16,294	(33,750)
Accounts payable	(69,608)	7,505
Accrued taxes	130,137	137,853
Collateral	(176,110)	229,746
Other current liabilities	35,647	21,829
Proceeds from the sale of real estate assets	27,144	15,020
Real estate investments	(94,533)	(59,527)
Change in risk management and trading liabilities	(132,540)	171,841
Change in other long-term assets	(6,609)	(909)
Change in other long-term liabilities	54,880	90,091
Net cash flow provided by operating activities	283,223	887,009
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(534,370)	(471,274)
Capitalized interest	(14,595)	(10,134)
Purchase of Sundance Plant		(185,046)
Proceeds from the sale of Silverhawk	207,620	
Proceeds from the sale of real estate investments	2,134	82,671
Proceeds from nuclear decommissioning trust sales	170,827	136,202
Investment in nuclear decommissioning trusts	(186,383)	(149,440)
Purchases of investment securities	(739,996)	(2,567,237)
Proceeds from sale of investment securities	536,679	2,679,691
Other	(2,246)	132
Net cash flow used for investing activities	(560,330)	(484,435)

CASH FLOWS FROM FINANCING ACTIVITIES

Issuance of long-term debt	703,283	911,815
Repayment of long-term debt	(384,800)	(734,163)
Short-term borrowings and payments net	41,659	(19,975)
Dividends paid on common stock	(148,876)	(137,234)
Common stock equity issuance	24,574	290,542
Other	15,486	(5,672)
Net cash flow provided by financing activities	251,326	305,313
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(25,781)	707,887
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	154,003	163,366
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 128,222	\$ 871,253

Supplemental disclosure of cash flow information

Cash paid during the period for:

Income taxes paid, net of refunds