PINNACLE WEST CAPITAL CORP

FORM 10-Q
(Quarterly Report)

Filed 08/14/98 for the Period Ending 06/30/98

Address	400 NORTH FIFTH STREET MS8695 PHOENIX, AZ 85004
Telephone	602 250 1000
CIK	0000764622
Symbol	PNW
SIC Code	4911 - Electric Services
Industry	Electric Utilities
Sector	Utilities
Fiscal Year	12/31

PINNACLE WEST CAPITAL CORP

FORM 10-Q
(Quarterly Report)

Filed 8/14/1998 For Period Ending 6/30/1998

Address	400 NORTH FIFTH STREET .
	PHOENIX, Arizona 85004
Telephone	602-379-2500
CIK	0000764622
Industry	Electric Utilities
Sector	Utilities
Fiscal Year	12/31

FORM 10-Q
Securities and Exchange Commission
Washington, D.C. 20549

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 1998

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ------------------ to --------------------

Commission file number 1-8962

PINNACLE WEST CAPITAL CORPORATION
(Exact name of registrant as specified in its charter)

Arizona	86-0512431
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
400 E. Van Buren St., P.O. Box 52132, Phoenix, Arizona	85072-2132
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (602) 379-2500

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Number of shares of common stock, no par value, outstanding as of August 12, 1998: 84,740,070

Glossary

ACC - Arizona Corporation Commission

ACC Staff - Staff of the Arizona Corporation Commission

APS - Arizona Public Service Company

Company - Pinnacle West Capital Corporation

DOE - United States Department of Energy

EITF - Emerging Issues Task Force

EITF 97-4 - Emerging Issues Task Force Issue No. 97-4, "Deregulation of the Pricing of Electricity --- Issues Related to the Applications of FASB Statements No. 71, Accounting for the Effects of Certain Types of Regulation, and No. 101, Regulated Enterprises --- Accounting for the Discontinuation of Application of FASB Statement No. 71"

El Dorado - El Dorado Investment Company

EPA - United States Environmental Protection Agency

FERC - Federal Energy Regulatory Commission

ITC - Investment tax credit

1997 10-K - Pinnacle West Capital Corporation Annual Report on Form 10-K for the fiscal year ended December 31, 1997

Palo Verde - Palo Verde Nuclear Generating Station

Pinnacle West - Pinnacle West Capital Corporation

Power Coordination Agreement - 1955 agreement between the Company and Salt River Project that provides for certain electric system and power sales

SFAS No. 71 - Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation"

SFAS No. 128 - Statement of Financial Accounting Standards No. 128, "Earnings Per Share"

SFAS No. 131 - Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information"

SFAS No. 133 - Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities"

Salt River Project - Salt River Project Agricultural Improvement and Power District

SunCor - SunCor Development Company

Territorial Agreement - 1955 agreement between APS and Salt River Project that has provided exclusive retail service territories in Arizona as against each other

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

PINNACLE WEST CAPITAL CORPORATION CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Dollars in thousands, except per share amounts)

	Three Months Ended June 30, 1998	Three Months Ended June 30, 1997
Operating Revenues		
Electric	$ 441,715	$ 458,751
Real estate	28,916	30,166
Total	470,631	488,917
Fuel Expenses		
Fuel for electric generation	50,434	55,626
Purchased power	45,151	43,684
Total	95,585	99,310
Operating Expenses		
Utility operations and maintenance	102,713	89,162
Real estate operations	26,213	28,301
Depreciation and amortization	93,585	91,809
Taxes other than income taxes	29,930	30,311
Total	252,441	239,583
Operating Income	122,605	150,024
Other Income (Deductions)		
Interest on long-term debt	(38,067)	(41,232)
Other interest	(4,374)	(5,973)
Capitalized interest	4,874	5,339
Preferred stock dividend requirements of APS	(2,435)	(3,195)
Other - net	192	4,823
Total	(39,810)	(40,238)
Income Before Income Tax	82,795	109,786
Income Tax Expense	33,798	42,604
Net Income	$ 48,997	$ 67,182
Average Common Shares Outstanding	84,810,790	85,155,688
Earnings Per Average Common Share Outstanding:		
Net income - basic	$ 0.58	$ 0.79
Net income - diluted	$ 0.57	$ 0.78
Dividends Declared Per Share	$ 0.600	$ 0.550

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Dollars in thousands, except per share amounts)

	Six Months Ended June 30, 1998	Six Months Ended June 30, 1997
Operating Revenues		
Electric	$ 822,138	$ 837,772
Real estate	63,077	49,709
Total	885,215	887,481
Fuel Expenses		
Fuel for electric generation	100,762	106,748
Purchased power	68,740	78,031
Total	169,502	184,779
Operating Expenses		
Utility operations and maintenance	199,129	177,178
Real estate operations	56,449	48,063
Depreciation and amortization	186,415	184,411
Taxes other than income taxes	60,278	60,555
Total	502,271	470,207
Operating Income	213,442	232,495
Other Income (Deductions)		
Interest on long-term debt	(78,282)	(81,520)
Other interest	(7,081)	(10,474)
Capitalized interest	9,530	10,010
Preferred stock dividend requirements of APS	(5,313)	(6,821)
Other - net	4,551	9,046
Total	(76,595)	(79,759)
Income Before Income Tax	136,847	152,736
Income Tax Expense	56,764	60,172
Net Income	$ 80,083	$ 92,564
Average Common Shares Outstanding	84,798,120	86,280,924
Earnings Per Average Common Share Outstanding:		
Net Income - Basic	$ 0.94	$ 1.07
Net Income - Diluted	$ 0.94	$ 1.07
Dividends Declared Per Share	$ 0.900	$ 0.825

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Dollars in thousands, except per share amounts)

	Twelve Months Ended June 30, 1998	Twelve Months Ended June 30, 1997
Operating Revenues		
Electric	$ 1,862,919	$ 1,784,125
Real estate	129,841	107,053
Total	1,992,760	1,891,178
Fuel Expenses		
Fuel for electric generation	195,355	237,518
Purchased power	225,995	136,757
Total	421,350	374,275
Operating Expenses		
Utility operations and maintenance	421,385	419,853
Real estate operations	120,014	100,790
Depreciation and amortization	370,289	365,641
Taxes other than income taxes	121,269	112,921
Total	1,032,957	999,205
Operating Income	538,453	517,698
Other Income (Deductions)		
Allowance for equity funds used during construction	--	1,531
Interest on long-term debt	(160,927)	(164,502)
Other interest	(15,280)	(23,191)
Capitalized interest	19,223	16,226
Preferred stock dividend requirements of APS	(11,295)	(15,110)
Other - net	74	1,611
Total	(168,205)	(183,435)
Income From Continuing Operations Before Income Tax	370,248	334,263
Income Tax Expense	146,873	126,953
Income From Continuing Operations	223,375	207,310
Loss from Discontinued Operations, Net of Income Tax of $6,461	--	(9,539)
Extraordinary Charge for Early Retirement of Debt, Net of Income Tax of $9,667	--	(14,272)
Net Income	$ 223,375	$ 183,499
Average Common Shares Outstanding	84,767,601	86,869,084
Earnings Per Average Common Share Outstanding:		
Continuing Operations - Basic	$ 2.64	$ 2.38
Net Income - Basic	$ 2.64	$ 2.11
Continuing Operations - Diluted	$ 2.62	$ 2.37
Net Income - Diluted	$ 2.62	$ 2.10
Dividends Declared Per Share	$ 1.200	$ 1.100

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

ASSETS
(Thousands of Dollars)

	June 30, 1998	December 31, 1997
Current Assets		
Cash and cash equivalents	$ 31,641	$ 27,484
Customer and other receivables - net	170,963	183,507
Accrued utility revenues	66,922	58,559
Material and supplies	71,207	70,634
Fossil fuel	17,960	9,621
Deferred income taxes	35,401	57,887
Other current assets	46,722	41,408
Total current assets	440,816	449,100
Investments and Other Assets		
Real estate investments - net	349,951	365,921
Other assets	226,171	215,027
Total investments and other assets	576,122	580,948
Utility Plant		
Electric plant in service and held for future use	7,057,168	7,009,059
Less accumulated depreciation and amortization	2,720,762	2,620,607
Total	4,336,406	4,388,452
Construction work in progress	294,978	237,492
Nuclear fuel, net of amortization	51,165	51,624
Net utility plant	4,682,549	4,677,568
Deferred Debits		
Regulatory asset for income taxes	430,601	458,369
Rate synchronization cost deferrals	331,265	358,871
Other deferred debits	310,516	325,561
Total deferred debits	1,072,382	1,142,801
Total Assets	$6,771,869	$6,850,417

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

LIABILITIES AND EQUITY
(Thousands of Dollars)

	June 30, 1998	December 31, 1997
Current Liabilities		
Accounts payable	$ 106,327	$ 117,429
Accrued taxes	76,863	84,610
Accrued interest	32,625	32,974
Dividends payable	25,445	--
Short-term borrowings	213,485	130,750
Current maturities of long-term debt	158,077	108,695
Customer deposits	31,024	30,672
Other current liabilities	22,896	18,534
Total current liabilities	666,742	523,664
Long-Term Debt Less Current Maturities	2,075,107	2,244,248
Deferred Credits and Other		
Deferred income taxes	1,343,658	1,363,461
Deferred investment tax credit	42,966	50,861
Unamortized gain - sale of utility plant	80,075	82,363
Other	392,386	387,223
Total deferred credits and other	1,859,085	1,883,908
Commitments and Contingencies (Notes 5, 8 and 9)		
Minority Interests		
Non-redeemable preferred stock of APS	124,034	142,051
Redeemable preferred stock of APS	15,377	29,110
Common Stock Equity		
Common stock, no par value	1,554,097	1,553,771
Retained earnings	477,427	473,665
Total common stock equity	2,031,524	2,027,436
Total Liabilities and Equity	$6,771,869	$6,850,417

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(THOUSANDS OF DOLLARS)

	Six Months Ended June 30, 1998	Six Months Ended June 30, 1997
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 80,083	$ 92,564
Items not requiring cash		
Depreciation and amortization	203,388	200,991
Deferred income taxes - net	5,645	(24,844)
Deferred investment tax credit	(7,895)	(7,870)
Other - net	389	(10,123)
Changes in current assets and liabilities		
Customer and other receivables - net	12,544	(2,296)
Accrued utility revenues	(8,363)	(14,047)
Materials, supplies and fossil fuel	(8,912)	1,153
Other current assets	(5,314)	(4,222)
Accounts payable	(12,438)	(39,477)
Accrued taxes	(8,081)	33,387
Accrued interest	(349)	(5,181)
Other current liabilities	5,339	(10,838)
Decrease in land held	15,084	6,189
Other - net	4,686	29,820
Net Cash Flow Provided By Operating Activities	275,806	245,206
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(144,580)	(145,203)
Capitalized interest	(9,530)	(8,394)
Other - net	3,435	(2,389)
Net Cash Flow Used For Investing Activities	(150,675)	(155,986)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	99,375	102,382
Short-term borrowings - net	82,735	211,100
Dividends paid on common stock	(50,878)	(47,441)
Repayment of long-term debt	(220,782)	(230,823)
Redemption of preferred stock	(31,209)	(46,044)
Repurchase and retirement of common stock	--	(79,863)
Other - net	(215)	(176)
Net Cash Flow Used For Financing Activities	(120,974)	(90,865)
Net Cash Flow	4,157	(1,645)
Cash and Cash Equivalents at Beginning of Period	27,484	26,686
Cash and Cash Equivalents at End of Period	$ 31,641	$ 25,041
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for:		
Interest, net of amounts capitalized	$ 72,863	$ 83,351
Income taxes	$ 64,820	$ 56,090

See Notes to Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. The condensed consolidated financial statements include the accounts of Pinnacle West and its subsidiaries: APS, SunCor and El Dorado. All significant intercompany balances have been eliminated. Certain prior year balances have been restated to conform to the current year presentation.

2. In the opinion of the Company, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of normal recurring accruals) necessary to present fairly the financial position of Pinnacle West and its subsidiaries as of June 30, 1998, the results of operations for the three months, six months and twelve months ended June 30, 1998 and 1997, and the cash flows for the six months ended June 30, 1998 and 1997. It is suggested that these condensed consolidated financial statements and notes to condensed consolidated financial statements be read in conjunction with the consolidated financial statements and notes to consolidated financial statements included in the 1997 10-K.

3. The operations of APS are subject to seasonal fluctuations, with variations in energy usage by customers occurring from season to season and from month to month within a season, primarily as a result of changing weather conditions. For this and other reasons, the results of operations for interim periods are not necessarily indicative of the results to be expected for the full year.

4. See "Liquidity and Capital Resources" in Part I, Item 2 of this report for changes in capitalization for the six months ended June 30, 1998.

5. Regulatory Matters --- Electric Industry Restructuring

State

ACC Rules. In December 1996, the ACC adopted rules that provide a framework for the introduction of retail electric competition in Arizona. On August 5, 1998, the ACC adopted amendments to the rules. The ACC rules, as amended, include the following major provisions:

o The rules apply to virtually all of the Arizona electric utilities regulated by the ACC, including APS.

o The rules require each affected utility, including APS, to make available at least 20% of its 1995 system retail peak demand for competitive generation supply to all customer classes not later than January 1, 1999, and 100% no later than January 1, 2001.

o All affected utility customers with single premise loads of one megawatt or greater will be eligible for competitive electric services beginning January 1, 1999, until the 20% level described in the preceding paragraph is met. Until the 20% level is met, affected utility customers with single premise loads of forty kilowatts or greater will be able to aggregate into a combined load of one megawatt or greater to be eligible for competitive electric services beginning January 1, 1999.

o Prior to January 1, 2001, residential customers will have access to competitive services through a quarterly phase-in of one-half percent of residential customers per quarter beginning January 1, 1999.

o Electric service providers that obtain Certificates of Convenience and Necessity (CC&Ns) from the ACC will be allowed to supply, market, and/or broker specified electric services at retail. These services include electric generation, but exclude electric transmission and distribution.

o As required by the rules, in February 1998 APS filed with the ACC proposed tariffs for unbundled service (electric service elements provided and priced seperately). The ACC has not issued a decision in this matter.

o The rules establish that the ACC shall allow a reasonable opportunity for the recovery of unmitigated stranded costs. See "Stranded Costs" below. Affected utilities are expected to take reasonable, cost-effective steps to mitigate stranded costs.

o Absent a waiver from the ACC, each affected utility must separate itself from all competitive generation assets and services prior to January 1, 2001. The separation must be either to an unaffiliated party or to a separate corporate affiliate or affiliates.

o Beginning January 1, 1999, each affected utility will be prohibited from providing certain competitive electric services, except through a separate affiliate.

o The rules contain affiliate transaction rules generally prohibiting an affected utility and its competitive electric affiliates from sharing personnel, office space, equipment, services, and systems, except to the extent appropriate to perform certain permissible shared corporate support functions. No later than December 31, 1998, each affected utility must file a compliance plan with the ACC demonstrating its compliance with the affiliate transaction rules.

o By September 15, 1998, each affected utility must file a report detailing possible mechanisms to provide benefits, such as rate reductions of 3% to 5%, to all standard offer customers and a proposed plan for residential phase-in implementation.

The amended rules, a copy of which has been filed as an exhibit to this Report on Form

10-Q, became effective on an emergency basis upon their filing with the Secretary of State on August 10, 1998; however, the ACC must complete a public process to adopt the rules on a permanent basis within 180 days. The Company anticipates the completion of this process by year-end 1998 or early 1999.

The Company believes that certain provisions of the ACC rules are deficient. In February 1997, a lawsuit was filed by APS to protect its legal rights regarding those rules. That lawsuit is pending but two related cases filed by other utilities have been partially decided in a manner adverse to those utilities' positions.

Stranded Costs. In February 1998, the ACC completed a formal, generic hearing on stranded cost determination and recovery. On June 22, 1998, the ACC issued an order in this matter. The order allows an affected utility, such as APS, to choose between two options for the recovery of its stranded costs. Under the first option, an affected utility that chooses to divest its generating assets to an unaffiliated party must file a divestiture plan for ACC approval no later than October 1, 1998, and such divestiture must be completed by January 1, 2001, after which the affected utility would be permitted to collect 100 percent of its stranded costs, including a return on the unamortized balance, over a ten-year period. Under the second option (referred to by the ACC as the "Transition Revenues Methodology"), an affected utility would be provided sufficient revenues necessary to maintain financial integrity for a period of ten years or the ACC would "otherwise provide an allocation of stranded cost responsibilities and risks between ratepayers and shareholders as is determined to be in the public interest." The order also states an intent that the various recovery options "will provide the affected utilities sufficient revenues to enable them to recover appropriate regulatory assets." The order requires each affected utility to file with the ACC, on or before August 21, 1998, its choice of options for stranded cost recovery as well as an implementation plan relating to its chosen option, including its estimated stranded costs separated out into regulatory assets and other generation related assets. Stranded costs estimates vary depending on various assumptions, estimates, methodologies and measurement periods. Based on various assumptions, estimates and methodologies, APS has previously estimated that its recoverable stranded costs (excluding regulatory assets which have already been addressed in the 1996 regulatory agreement with the ACC) would be less than $500 million, assuming a measurement period 2001 through 2006.

APS intends to use the Transitional Revenues Methodology and does not intend to divest its generating assets to an unaffiliated party. The Company cannot accurately predict the outcome of this matter.

Legislative Initiatives. An Arizona joint legislative committee studied electric utility industry restructuring issues in 1996 and 1997. In conjunction with that study, Arizona legislative counsel prepared memoranda in late 1997 related to the legal authority of the ACC to deregulate the Arizona electric utility industry. The memoranda raise a question as to the degree to which the ACC may, under the Arizona Constitution, deregulate any portion of the electric utility industry and allow rates to be determined by market forces. This latter issue (the ability of the ACC to set rates based on the competitive market) has been subsequently decided in favor of the ACC in one unrelated and two related lawsuits.

In May 1998, a bill was enacted to facilitate implementation of retail electric competition in the state. The bill includes the following major provisions: (a) requirements that Arizona's largest government-operated electric utility (Salt River Project) and, at their option, smaller city electric systems (i) open their service territories to electric service providers to implement retail electric generation competition for 20% of each utility's 1995 retail peak demand by December 31, 1998 and for all retail customers by December 31, 2000;
(ii) decrease rates by at least 10% over a ten-year period beginning as early as January 1, 1991; (iii) implement procedures and public processes, including judicial review at the request of either an interested party or the Arizona Attorney General, for establishing the terms, conditions and pricing of electric services as well as certain other decisions affecting retail electric competition, which procedures and processes are comparable to those already applicable to public service corporations; (b) a description of the factors which form the basis of consideration by Salt River Project in determining stranded costs; and (c) a requirement that metering and meter reading services be provided on a competitive basis during the first two years of competition only for customers having demands in excess of one megawatt (and that are eligible for competitive generation services), and thereafter for all customers receiving competitive electric generation. In addition, the Arizona legislature will review and make recommendations for the 1999 legislature on certain competitive issues.

Federal

The Energy Policy Act of 1992 and recent rulemakings by FERC have promoted increased competition in the wholesale electric power markets. The Company does not expect these rules to have a material impact on its financial statements.

Several electric utility reform bills have been introduced during recent congressional sessions, which as currently written, would allow consumers to choose their electricity suppliers by 2000 or 2003. These bills, other bills that are expected to be introduced, and ongoing discussions at the federal level suggest a wide range of opinion that will need to be narrowed before any substantial restructuring of the electric utility industry can occur.

Regulatory Accounting

APS prepares its financial statements in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation." SFAS No. 71 requires a cost-based, rate-regulated enterprise to reflect the impact of regulatory decisions in its financial statements. APS' existing regulatory orders and current regulatory environment support its accounting practices related to regulatory assets, which amounted to approximately $0.9 billion at June 30, 1998. In accordance with the 1996 regulatory agreement, the ACC accelerated the amortization of substantially all of APS' regulatory assets to an eight-year period that began July 1, 1996.

During 1997, the Emerging Issues Task Force (EITF) of the Financial Accounting Standards Board (FASB) issued EITF 97-4, which requires that SFAS No. 71 be discontinued no later than when legislation is passed or a rate order is issued that contains sufficient detail to determine its effect on the portion of the business being deregulated, which could result in write-downs or write-offs of physical and/or regulatory assets. Additionally, the EITF determined that regulatory assets should not be written off if they are to be recovered from a portion of the entity which continues to apply SFAS No. 71.

Although the ACC has issued rules for transitioning generation services to competition, there are many unresolved issues. APS continues to apply SFAS No. 71 to all of its operations. If rate recovery of regulatory assets is no longer probable, whether due to competition or regulatory action, APS would be required to write off the remaining balance as an extraordinary charge to expense.

General

Changes in ACC decisions, Arizona and federal legislation, and possible amendments to the Arizona Constitution may impact the implementation of retail electric competition in Arizona. Until the details of implementation of competition, including addressing stranded costs, are determined, the Company cannot accurately predict the impact of full retail competition on its financial position, cash flows or results of operation. As competition in the electric industry continues to evolve, the Company will continue to evaluate strategies and alternatives that will position APS to compete in the new regulatory environment.

6. Regulatory Matters --- 1996 Regulatory Agreement

In April 1996, the ACC approved a regulatory agreement between APS and the ACC Staff. The major provisions of this agreement are:

o An annual rate reduction of approximately $48.5 million ($29 million after income taxes), or 3.4% on average for all customers except certain contract customers, effective July 1, 1996.

o Recovery of substantially all of APS' present regulatory assets through accelerated amortization over an eight-year period that began July 1, 1996, increasing annual amortization by approximately $120 million ($72 million after income taxes).

o A formula for sharing future cost savings between customers and shareholders (price reduction formula) referencing a return on equity (as defined) of 11.25%.

o A moratorium on filing for permanent rate changes prior to July 2, 1999, except under the price reduction formula and under certain other limited circumstances.

o Infusion of $200 million of common equity into APS by the parent company, in annual payments of $50 million starting in 1996.

Pursuant to the price reduction formula, in May 1997, the ACC approved a retail price decrease of approximately $17.6 million ($10.5 million after income taxes), or 1.2%, effective July 1, 1997. In March 1998, APS filed with the ACC its calculation of an annual price reduction of approximately $17 million ($10 million after income taxes), or 1.1%, to become effective July 1, 1998. The amount and timing of the price decrease are subject to ACC approval.

7. Agreement with Salt River Project

On April 25, 1998, APS and Salt River Project entered into a Memorandum of Agreement in anticipation of, and to facilitate, the opening of the Arizona electric industry. The Agreement contains the following major components:

o APS and Salt River Project would amend the Territorial Agreement to remove any barriers to the provision of competitive electricity supply and non-distribution services.

o APS and Salt River Project would amend the Power Coordination Agreement to lower the price that APS will pay Salt River Project for purchased power by approximately $17 million (pretax) in 1999 and by lesser annual amounts through 2006.

o APS and Salt River Project agreed on certain legislative positions regarding electric utility restructuring at the state and federal level.

An ACC docket had previously been established and the ACC held a hearing on August 6, 1998 so that the ACC could review certain provisions of the Memorandum of Agreement, as amended, including, whether: (a) the Territorial Agreement remains in the public interest, (b) the Agreement is a contract in restraint of trade, and (c) the Agreement will materially lessen the potential for retail electric competition in Arizona.

The Antitrust Unit of the Arizona Attorney General's Office, which has been involved in the ongoing regulatory and legislative proceedings regarding the restructuring of the Arizona electric industry, requested clarification of the operation of certain of the Agreement's provisions. Pursuant to an Addendum to Memorandum of Agreement, dated as of May 19, 1998 (the "Addendum"), APS and Salt River Project amended and clarified certain provisions of the Memorandum of Agreement in response to certain issues raised by the Antitrust Unit. By letter dated May 19, 1998, the Antitrust Unit advised APS and Salt River Project that, upon their execution of the Addendum, it would take no action regarding the language of the Memorandum of Agreement, although it reserved the right to take action in the future if new information justified doing so.

8. The Palo Verde participants have insurance for public liability payments resulting from nuclear energy hazards to the full limit of liability under federal law. This potential liability is covered by primary liability insurance provided by commercial insurance carriers in the amount of $200 million and the balance by an industry-wide retrospective assessment program. If losses at any nuclear power plant covered by the programs exceed the accumulated funds, APS could be assessed retrospective premium adjustments. The maximum assessment per reactor under the program for each nuclear incident is approximately $88 million, subject to an annual limit of $10 million per incident. Based upon APS' 29.1% interest in the three Palo Verde units, APS' maximum potential assessment per incident is approximately $77 million, with an annual payment limitation of approximately $9 million.

The Palo Verde participants maintain "all risk" (including nuclear hazards) insurance for property damage to, and decontamination of, property at Palo Verde in the aggregate amount of $2.75 billion, a substantial portion of which must first be applied to stabilization and decontamination. APS has also secured insurance against portions of any increased cost of generation or purchased power and business interruption resulting from a sudden and unforeseen outage of any of the three units. The insurance coverage discussed in this and the previous paragraph is subject to certain policy conditions and exclusions.

9. APS has encountered tube cracking in the Palo Verde steam generators and has taken, and will continue to take, remedial actions that it believes have slowed the rate of tube degradation. The projected service life of the steam generators is reassessed periodically and these analyses indicate that it will be economically desirable for APS to replace the Unit 2 steam generators between 2003 and 2008. APS estimates that its share of the replacement costs (in 1998 dollars) will be approximately $50 million, most of which will be incurred after the year 2000. During the fourth quarter of 1997, the Palo Verde participants, including APS, entered into a contract for the fabrication of two replacement steam generators. The cost to APS is estimated at approximately $26 million. These generators will be used as replacements if performance of existing generators deteriorates to less than acceptable levels. The generators are expected on site in 2002. APS' share of installation costs is approximately $24 million. Based on the latest available data, APS estimates that the Unit 1 and Unit 3 steam generators should operate for the license periods (until 2025 and 2027, respectively), although APS will continue its normal periodic assessment of these steam generators.

10. The Financial Accounting Standards Board issued SFAS No. 131 on "Disclosures about Segments of an Enterprise and Related Information" which is effective for fiscal years beginning after December 15, 1997. SFAS No. 131 requires that public companies report certain information about operating segments in their financial statements. It also establishes related disclosures about products and services, geographic areas, and major customers. The Company is currently evaluating what impact this standard will have on its disclosures.

In June 1998 the Financial Accounting Standards Board issued SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities," which is effective for the Company in 2000. SFAS No. 133 requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The standard also provides specific guidance for accounting for derivatives designated as hedging instruments. The Company is currently evaluating what impact this standard will have on its financial statements.

11. In 1997 the Company adopted SFAS No. 128 "Earnings Per Share." This statement requires the presentation of both basic and diluted earnings per share on the financial statements. The following table presents earnings per average common share outstanding (EPS):

	Twelve Months Ended June 30,	
Basic EPS:	1998	1997
Continuing operations	$2.64	$2.38
Discontinued operations	--	(0.11)
Extraordinary charge	--	(0.16)
Net Income	$2.64	$2.11
Diluted EPS		
Continuing operations	$2.62	$2.37
Discontinued operations	--	(0.11)
Extraordinary charge	--	(0.16)
Net Income	$2.62	$2.10

Dilutive stock options increased average common shares outstanding by 605,279 and 449,369 for the three-month period ended June 30, 1998 and 1997 respectively; 577,489 and 497,751 for the six-month period ended June 30, 1998 and 1997 respectively; and 530,970 and 568,532 for the twelve-month period ended June 30, 1998 and 1997 respectively, but had no effect on net income. Total average common shares outstanding for the purposes of calculating diluted earnings per share were 85,416,069 and 85,605,057 for the three-month period ended June 30, 1998 and 1997 respectively; 85,375,609 and 86,778,675 for the six-month period ended June 30, 1998 and 1997 respectively; and 85,298,570 and 87,437,615 for the twelve-month period ended June 30, 1998 and 1997 respectively.

PINNACLE WEST CAPITAL CORPORATION

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Operating Results

The following table shows the income and/or loss of Pinnacle West and its subsidiaries for the three-month, six-month and twelve-month periods ended June 30, 1998 and 1997:

Income (Loss)
(Unaudited)

(Thousands of Dollars)

	Three Months Ended June 30,		Six Months Ended June 30,		Twelve Months Ended June 30,	
	1998	1997	1998	1997	1998	1997
APS	$ 49,749	$ 66,298	$ 78,806	$ 91,317	$ 226,179	$ 210,453
SunCor	2,046	1,167	5,285	2,255	8,364	7,501
El Dorado	1,038	3,686	4,207	6,956	5,441	7,366
Pinnacle West (1)	(3,836)	(3,969)	(8,215)	(7,964)	(16,609)	(41,821)
Net Income	$ 48,997	$ 67,182	$ 80,083	$ 92,564	$ 223,375	$ 183,499

(1) Includes Pinnacle West's interest expense, extraordinary charge for early retirement of debt, discontinued operations and operating expenses net of income tax benefits. Income tax benefit (expenses) are as follows (in thousands):
$(539) and $822 for the three months ended June 30, 1998 and 1997, respectively; $(1,460) and $1,208 for the six months ended June 30, 1998 and 1997, respectively; and $82 and $17,678 for the twelve months ended June 30, 1998 and 1997, respectively.

APS

Operating Results - Three-month period ended June 30, 1998 compared with three-month period ended June 30, 1997

Earnings decreased $17 million in the three-month comparison primarily because of the effects of weather, increased operations and maintenance expenses, and a retail price reduction, partially offset by customer growth and lower fuel expenses. See Note 6 of Notes to Condensed Consolidated Financial Statements for information on the price reduction.

Operating revenues decreased $17 million because of weather effects ($41 million) and the price reduction ($4 million), partially offset by the effects of customer growth ($17 million), increased sales for resale ($8 million) and other ($3 million). Sales for resale are wholesale electricity sales to third parties who resell the electricity to their customers. The increase in sales for resale was a result of changes in power marketing activity, which can vary from period to period without corresponding effects on earnings because of related fluctuations in purchased power costs.

Operations and maintenance expenses increased $14 million as a result of the timing of scheduled outages at power plants and other miscellaneous expenses.

Fuel expenses decreased $4 million primarily because of lower fuel prices and lower retail sales, partially offset by higher sales for resale.

Operating Results - Six-month period ended June 30, 1998 compared with six-month period ended June 30, 1997

Earnings decreased $13 million in the six-month comparison primarily because of the effects of weather, increased operations and maintenance expenses, and a retail price reduction, partially offset by customer growth and lower fuel expenses. See Note 6 of Notes to Condensed Consolidated Financial Statements for additional information about the price reduction.

Operating revenues decreased $16 million because of weather effects ($38 million) and the price reduction ($8 million), partially offset by the effects of customer growth ($29 million). Operations and maintenance expenses increased $22 million as a result of growth and increased expenses due to impending competition, the timing of scheduled outages at power plants and other miscellaneous factors.

Fuel expenses decreased $15 million primarily because of lower prices and a more favorable mix.

Operating Results - Twelve-month period ended June 30, 1998 compared with twelve-month period ended June 30, 1997

Earnings increased $16 million in the twelve-month comparison primarily because of customer growth; two fuel-related settlements in the third quarter of 1997; and lower fuel prices. These positive factors more than offset the effects of weather and a retail price reduction. See Note 6 of Notes to Condensed Consolidated Financial Statements for additional information about the price reduction. In the period ended June 30, 1997, APS also recognized $8 million of income tax benefits associated with capital loss carryforwards.

Operating revenues increased $79 million primarily because of increases in sales for resale ($80 million) and customer growth ($57 million), partially offset by the effects of weather ($37 million) and the price reduction ($18 million). Sales for resale are wholesale electricity sales to third parties who resell the electricity to their customers. The increase in sales for resale was a result of changes in power marketing activity, which can vary from period to period without corresponding effects on earnings because of related fluctuations in purchased power costs.

The two fuel-related settlements increased APS' pretax earnings by approximately $21 million. The Company's consolidated income statement reflects these settlements as reductions in fuel expense and as other income.

Operations and maintenance expenses increased $2 million because higher expenses related to growth and impending competition, the timing of scheduled outages at power plants and other miscellaneous factors more than offset the effects of a charge for a voluntary severance program recorded in 1996 and related savings in 1997.

Non-Utility Operations

The parent company's losses decreased in the twelve-month period due to lower interest expense resulting from debt reduction. The twelve-month period ended June 30, 1997 includes extraordinary charges related to the early retirement of debt and a loss from discontinued operations on a legal matter related to MeraBank, A Federal Savings Bank (a former subsidiary).

SunCor's earnings increased in all periods because of an increase in net land and home sales.

El Dorado's decreased earnings are the result of investment sales in periods ended 1997.

Investment Tax Credit Amortization

As part of a 1994 rate settlement with the ACC, the Company accelerated amortization of substantially all deferred ITCs over a five-year period that ends on December 31, 1999. The amortization of ITCs decreases annual consolidated income tax expense by approximately $24 million.

Liquidity and Capital Resources

Parent Company

The parent company's cash requirements and its ability to fund those requirements are discussed under "Capital Needs and Resources" in Management's Discussion and Analysis of Financial Condition and Results of Operation in Part II, Item 7 of the 1997 10-K.

During the six-months ended June 30, 1998, the parent company redeemed approximately $54 million of its long-term debt with cash from operations and short-term borrowings.

As a result of the 1996 regulatory agreement (see Note 6 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report), the parent company has invested $50 million in APS in 1996 and 1997 and will invest similar amounts annually in 1998 and 1999.

The Board declared a quarterly dividend of 30 cents per share of common stock, payable September 1, 1998 to shareholders of record on August 1, 1998, totaling approximately $ 25.4 million.

APS

For the six months ended June 30, 1998, APS incurred approximately $145 million in capital expenditures, which is approximately 45% of the most recently estimated 1998 capital expenditures. APS' projected capital expenditures for the next three years are: 1998, $323 million; 1999, $322 million; and 2000, $317 million, respectively. These amounts include about $30 - $35 million each year for nuclear fuel expenditures. In addition, APS is considering expanding certain of its businesses over the next several years, which may result in increased expenditures.

APS' long-term debt and preferred stock redemption requirements and payment obligations on a capitalized lease for the next three years are: 1998, $176 million; 1999, $174 million; and 2000, $109 million. During the six months ended June 30, 1998, APS redeemed approximately $142 million of its long-term debt and approximately $31 million of its preferred stock with cash from operations and long-term and short-term debt. As a result of the 1996 regulatory agreement (see Note 6 of Notes to Condensed Consolidated Financial Statements), the parent company invested $50 million in APS in 1996 and 1997 and will invest similar amounts annually in 1998 and 1999.

Although provisions in APS' bond indenture, articles of incorporation, and financing orders from the ACC establish maximum amounts of additional first mortgage bonds and preferred stock that APS may issue, management does not expect any of these restrictions to limit APS' ability to meet its capital requirements.

Year 2000 Issue

As the year 2000 approaches many companies face problems because many software application and operational programs will not properly recognize calendar dates beginning with the year 2000. The Company and its subsidiaries are addressing the Year 2000 issue as described below.

APS

APS initiated a comprehensive company-wide Year 2000 program over a year ago to review and resolve all Year 2000 issues in critical systems and equipment in a timely manner in an effort to ensure the reliability of electric service to its customers. This included a company-wide awareness program of the Year 2000 issue.

APS believes that substantially all of its major information technology (IT) systems are Year 2000 compliant. APS has made, and will continue to make, certain modifications to its computer hardware and software systems and applications in an effort to ensure they are capable of handling changing business needs, including dates in the year 2000 and thereafter. In addition, other IT systems and non-IT systems, including embedded technology and real-time process control systems, are being analyzed for potential modifications. To date, APS has inventoried essentially all critical IT and non-IT systems and the assessment of these systems is ongoing. The analysis of the IT and non-IT systems should be complete in late 1998 and any renovation, validation and implementation to be made will be completed by mid-1999 for all critical systems that effect operations, except for those items that can only be completed during maintenance outages at Palo Verde, which will be completed during the last half of 1999. APS has also designated an internal audit/quality review team that is reviewing the individual Year 2000 projects and their Year 2000 readiness on a quarterly basis. The cost to APS of Year 2000 remediation has not had, and is not expected to have, a material adverse effect on APS' financial position, cash flows, or results of operations.

APS is in the process of communicating with its significant suppliers, business partners, other utilities and large customers to determine the extent to which it may be affected by these third parties' plans to remediate their own Year 2000 issues in a timely manner. APS has been interfacing with suppliers for systems, services and materials in order to assess whether their schedules for analysis and remediation of Year 2000 issues are timely and to assess their ability to continue to supply services and materials required by APS. However, APS cannot currently predict the effect on APS if the systems of these other companies are not Year 2000 compliant.

Parent Company and Non-Utility Subsidiaries

The parent company, SunCor, and El Dorado have made, and will continue to make, certain modifications to their respective computer hardware and software systems and applications in an effort to ensure they are capable of handling dates in the year 2000 and thereafter. The cost to the parent company, SunCor and El Dorado of Year 2000 remediation has not had, and is not expected to have, a material adverse effect on the Company's financial position, cash flows, or results of operations.

Competition and Electric Industry Restructuring

See Note 5 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for discussions of competitive developments and regulatory accounting. See Note 7 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of a proposed amendment to a Power Coordination Agreement with Salt River Project that APS estimates would reduce its pretax costs for purchased power by approximately $17 million in 1999 and by lesser annual amounts through 2006.

Rate Matters

See Note 6 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of a proposed price reduction.

Forward-Looking Statements

The above discussion contains forward-looking statements that involve risks and uncertainties. Words such as "estimates," "expects," "anticipates," "plans," "believes," "projects," and similar expressions identify forward-looking statements. These risks and uncertainties include, but are not limited to, the ongoing restructuring of the electric industry; the outcome of the regulatory proceedings relating to the restructuring; regulatory, tax and environmental legislation; the ability of APS to successfully compete outside its traditional regulated markets; regional economic conditions, which could affect customer growth; the cost of debt and equity capital; weather variations affecting customer usage; technological developments in the electric industry; and Year 2000 issues.

These factors and the other matters discussed above may cause future results to differ materially from historical results, or from results or outcomes currently expected or sought by the Company.

PART II - OTHER INFORMATION

ITEM 4. Submission of Matters to a Vote of Security Holders

At the Company's Annual Meeting of Shareholders held on May 20, 1998, the following persons were elected Class I Directors with a term to expire at the 2001 annual meeting:

	Votes For	Votes Against	Abstentions and Broker Non Votes
Roy A. Herberger, Jr.	78,660,794	890,545	N/A
George A. Schreiber, Jr.	78,708,165	843,174	N/A
Humberto S. Lopez	78,641,695	909,644	N/A

The following information relates primarily to Pinnacle West and its principal subsidiary APS.

ITEM 5. Other Information

EPA Environmental Regulation

As previously reported, the EPA has been considering the Grand Canyon Visability Transport Commission's recommendations prior to promulgating final regulations on a regional haze regulatory program and final regulations were expected by June 1998. See "Environmental Matters - EPA Environmental Regulation" in Part I, Item 1 of the 1997 10-K. These final regulations are now expected by December 1998. APS cannot currently estimate the capital expenditures, if any, which may be required as a result of the EPA studies and the Commission's recommendations.

As previously reported, in July 1997, the EPA promulgated final National Ambient Air Quality Standards for ozone and particulate matter. See "Environmental Matters - EPA Environmental Regulation" in Part I, Item 1 of the 1997 10-K. Congress recently enacted legislation that could delay the implementation of the regional haze requirements and particulate matter ambient standard.

Spent Nuclear Fuel and Waste Disposal

As previously reported, in November 1997, the D.C. Circuit issued a Writ of Mandamus precluding DOE from excusing its delay in accepting spent nuclear fuel by January 31, 1998. See "Generating Fuel and Purchased Power - Nuclear Fuel Supply - Spent Nuclear Fuel and Waste Disposal" in Part I, Item 1 of the 1997 10-K. On May 5, 1998, the D.C. Circuit issued a ruling refusing to order DOE to begin moving spent nuclear fuel. On July 24, 1998, APS filed a Petition for Review with the D.C. Circuit regarding DOE's obligation to begin accepting spent nuclear fuel. Arizona Public Service Company v. Department of **Energy and United States of America, No. 98-1346 (D.C. Cir.).**

Palo Verde Nuclear Generating Station

See Note 9 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of issues regarding the Palo Verde steam generators.

Construction and Financing Programs

See "Liquidity and Capital Resources" in Part I, Item 2 of this report for a discussion of the Company's construction and financing programs.

Competition and Electric Industry Restructuring

See Note 5 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of competition and the rules regarding the introduction of retail electric competition in Arizona. On February 28, 1997, a lawsuit was filed by APS to protect its legal rights regarding the rules and in its complaint APS asked the Court for (i) a judgment vacating the retail electric competition rules, (ii) a declaratory judgment that the rules are unlawful because, among other things, they were entered into without proper legal authorization, and (iii) a permanent injunction barring the ACC from enforcing or implementing the rules and from promulgating any other regulations without lawful authority.

ITEM 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit No.	Description
27.1	Financial Data Schedule

In addition to those Exhibits shown above, the Company hereby incorporates the following Exhibits pursuant to Exchange Act Rule 12b-32 and Regulation section 229.10(d) by reference to the filings set forth below:

Exhibit No.	Description	Originally Filed as Exhibit:	File No.[a]	Date Effective
10.1	Retail Electric Competition Rules	10.1 to APS' June 30, 1998 Form 10-Q Report	1-4473	8-14-98
10.2	Arizona Corporation Commission Order, Decision No. 59943, Dated December 26, 1996, including the rules regarding the introduction of retail competition in Arizona	99.1 to APS' 1996 Form 10-K Report	1-4473	3-28-97
10.3	Articles of Incorporation, restated as of July 29, 1988	19.1 to the Company's September 30, 1988 Form 10-Q Report	1-8962	11-14-88
10.4	Bylaws, amended as of February 21, 1996	3.1 to the Company's 1995 Form 10-K Report	1-8962	4-1-96

(b) Reports on Form 8-K

During the quarter ended June 30, 1998, and the period from July 1 through August 14, 1998, the Company filed the following reports on Form 8-K:

Report dated August 5, 1998 regarding the ACC rules related to retail competition.

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

SIGNATURES

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

PINNACLE WEST CAPITAL CORPORATION
(Registrant)

Dated: August 14, 1998 By: George A. Schreiber, Jr. George A. Schreiber, Jr.

Executive Vice President and
Chief Financial Officer
(Principal Financial Officer
and Officer Duly Authorized

to sign this Report)

ARTICLE UT

MULTIPLIER: 1,000

CURRENCY: U.S. DOLLARS

PERIOD TYPE	6 MOS
FISCAL YEAR END	DEC 31 1998
PERIOD START	JAN 01 1998
PERIOD END	JUN 30 1998
EXCHANGE RATE	1
BOOK VALUE	PER BOOK
TOTAL NET UTILITY PLANT	4,682,549
OTHER PROPERTY AND INVEST	576,122
TOTAL CURRENT ASSETS	440,816
TOTAL DEFERRED CHARGES	1,072,382
OTHER ASSETS	0
TOTAL ASSETS	6,771,869
COMMON	1,554,097
CAPITAL SURPLUS PAID IN	0
RETAINED EARNINGS	477,427
TOTAL COMMON STOCKHOLDERS EQ	2,031,524
PREFERRED MANDATORY	15,377
PREFERRED	124,034
LONG TERM DEBT NET	2,075,107
SHORT TERM NOTES	0
LONG TERM NOTES PAYABLE	0
COMMERCIAL PAPER OBLIGATIONS	213,485
LONG TERM DEBT CURRENT PORT	158,077
PREFERRED STOCK CURRENT	0
CAPITAL LEASE OBLIGATIONS	0
LEASES CURRENT	0
OTHER ITEMS CAPITAL AND LIAB	2,154,265
TOT CAPITALIZATION AND LIAB	6,771,869
GROSS OPERATING REVENUE	885,215
INCOME TAX EXPENSE	56,764
OTHER OPERATING EXPENSES	502,271
TOTAL OPERATING EXPENSES	671,773
OPERATING INCOME LOSS	213,442
OTHER INCOME NET	(76,595)
INCOME BEFORE INTEREST EXPEN	0
TOTAL INTEREST EXPENSE	75,833
NET INCOME	80,083
PREFERRED STOCK DIVIDENDS	0
EARNINGS AVAILABLE FOR COMM	80,083
COMMON STOCK DIVIDENDS	50,878
TOTAL INTEREST ON BONDS	58,953
CASH FLOW OPERATIONS	275,806
EPS PRIMARY	0.94
EPS DILUTED	0.94

End of Filing