

The Dawning of a New Era



ARIZONA POWER AUTHORITY 2017 ANNUAL REPORT—NO. 59



Presentation of Report

COMMISSION

May 2018

Dalton H. Cole

Chairman

10/1/2016-9/30/2017

The Arizona Power Authority (Authority) presents the Operating Year 2017 Annual Report. This report accounts for the Authority's operational and financial activities for the operating year ending September 30, 2017. It also covers the Authority's administration of Arizona's hydroelectric power entitlement generated at Hoover Dam and Powerplant.

Russell L. Jones

Vice Chairman

10/1/2016-9/30/2017

In preparation for a new contract, the Authority took time to review its Strategic Mission and Vision. After the addition of a permanent Executive Director and upon consultation with the customers, the Mission and Vision was revised and a set of Values was established. These Values are;

Stephen M. Brophy

10/1/2016-9/30/2017

1. Fiscal Responsibility
2. Cost Causation
3. Resource Focus
4. Customer Service
5. Creative Development

John F. Sullivan

5/1/2017-9/30/2017

Lawrence V.

Robertson, Jr.

5/1/2017-9/30/2017

While the Colorado River is still considered in a drought, we did experience an above average rainfall in 2017. While the Authority can't impact the drought, we can strive for operational excellence and control costs in the face of reduced energy estimates.

STAFF

Ed Gerak

Executive Director

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John T. Underhill, Jr.

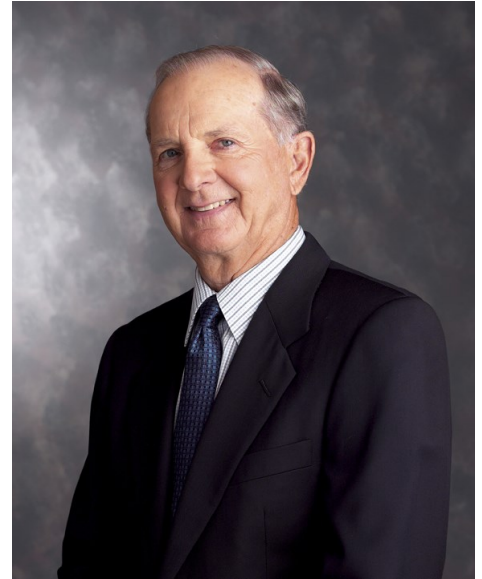
Interim Deputy Director



Commissioners

Dalton H. Cole—Chairman

Appointed to the Commission in January 2002 and re-appointed through his present term expiring in 2020, Dalton assumed the Chairman's role in September 2016. He is a retired businessman and farmer. A past member of the Central Arizona Water Conservation District Board, Mr. Cole co-founded and chaired the HoHoKam Irrigation District. He also served on the board of Electrical District No. 2 in Pinal County for 18 years and is a past chairman. In addition, Mr. Cole is a past chairman of the State Board of Directors for Community Colleges. He has served on the Ground Water Management Committee for Pinal County, as well as advisory committees to the Arizona Legislature regarding water and power issues.

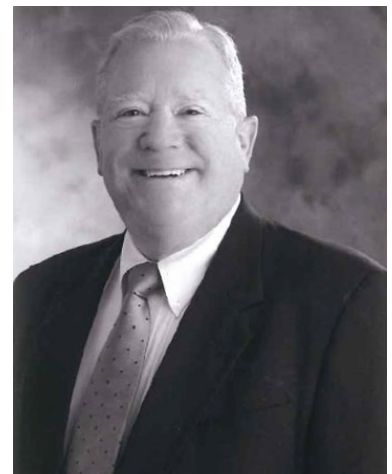


Stephen M. Brophy—Commissioner

Appointed to the Commission in 2009 and re-appointed through his present term expiring in 2020, Stephen M. Brophy is president of Page Land & Cattle Co., Aztec Land and Cattle Company, Ltd., the Apache Railway Co., and a partner in Santa Lucia Farms. Among his affiliations, he is a member of the boards of the Arizona Cattle Growers Association, Mountain States Legal Foundation, The National Cowboy Museum and former Chairman and member of the Economic Advisory Council of the Federal Bank of San Francisco. He received a bachelor's degree from the University of Arizona and an MBA from Stanford University.

Russel L. Jones— Vice Chairman

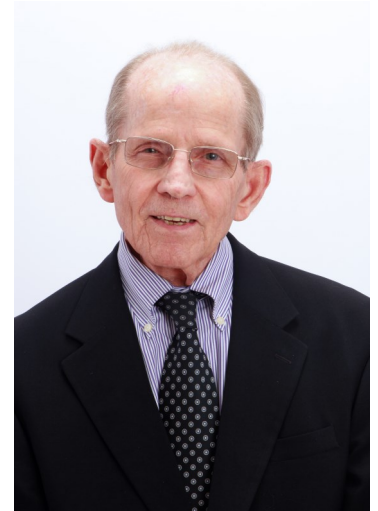
Appointed to the Commission in 2014, for a term expiring in 2018, Russ assumed the role of Vice Chairman in September 2016. He is the Chairman of the Board of R.L. Jones Management Group and R.L. Jones Custom Brokers, with seven (7) offices, serving key Ports of Entry along the U.S./Mexican Border, established in 1938 by his grandfather. Russ served three (3) terms in the Arizona House of Representatives, where he was the Chairman of the Agriculture and Water Committee. As well as holding a National Customs Broker license, he is a licensed Surplus Lines Insurance Broker, and sits on the executive committee and boards of several organizations; including the Arizona/Mexico Commission and Chairman of the Border Trade Alliance. An active Rotarian and pilot in the Civil Air Patrol, Russ is also a proud member of VFW Post 19 in Yuma.



Commissioners

Lawrence V. Robertson, Jr. —Commissioner

Appointed to the Commission in 2017 for a term expiring in 2022, Larry V. Robertson, Jr. is a natural resource, utility and energy attorney, of counsel with Munger-Chadwick . Admitted to the Arizona Bar in 1964, Larry has worked as Secretary and General Counsel for Southwest Gas Corporation; Vice President and General Attorney, Tucson Electric Power Company; Vice-President, Secretary and General Counsel, Interstate Natural Gas Association of America; Undersecretary of Energy and Deputy General Counsel for the U.S. Department of Energy. Larry has also been admitted to the Nevada, Wyoming, Montana, Texas and Colorado bars, as well as the U.S. District Court and the U.S. Supreme Court. He received a bachelor's degree and Juris Doctor from Stanford University.



John F. Sullivan —Commissioner

Appointed to the Commission in 2017 for a term expiring in 2022, John F. Sullivan is the former Deputy General Manager and Chief Strategic Initiatives Executive of the Salt River Project. His areas of responsibilities included Energy Management, Water Resource Management, and Strategic Planning. Prior to this John served for 2 ½ years as Associate General Manager and Chief Resources Executive and 17 years as Salt River Project's Associate General Manager for the Water Group. John received his baccalaureate degree in electrical engineering from the University of Arizona, is a past President of the Water for the West Foundation, Colorado River Water Users Association, Colorado River Energy Distributors Association and the National Water Resource Association.

Staff



Staff (From Left to Right)

Abel Gunn— Senior Accountant

Heather Cole—Executive Secretary

Linda Sullivan —Senior Rate Analyst

Gary Kern—Financial Administrator

Ed Gerak—Executive Director

Robert Nieto—IT Manager

Chris Shoop—Senior Rate Analyst

Report of the Executive Director

At the end of the 2016 operating year, all the hard work from the reallocation process came to fruition with the signing of the new 50 Year Hoover contracts with 63 customers. While our customers celebrated the signing of those contracts, the Arizona Power Authority was already turning the page in preparation of the next phase in the process: implementation. Staff and Commissioners went to work on multiple items that needed to be finalized after the signing of the contracts.

To evaluate the effectiveness of the Arizona Power Authority and to chart a course for the future a strategic planning session was held at Hoover Dam in September of 2016. The most important item coming out of the session was the immediate search for an Executive Director, given that the agency had been headed up by consultants for the previous 1 1/2 years. This was completed in April 2017 with the hiring of Ed Gerak as the new Executive Director.

During the reallocation process, an Arizona Auditor General Performance Audit also was initiated and the results were released in December of 2016. The recommendations from that report were minor procedural improvements, and the Commission had fixed three of the four issues, by resolution, prior to the final report being released. The fourth issue, a formal power pooling program, was finalized in May of 2017, but could not be executed until the new contracts took effect in October of 2017.



Before the contracts could take effect, some items needed to be finalized. Besides the power pooling program, the Arizona Power Authority issued a RFP for a Scheduling Entity Agreement. The Authority received three responses to the RFP and upon request from certain customers, an exception was made to include Western Area Power Authority (since they could not respond to a state based RFP due to government procurement limitations). We entered into Scheduling Entity Agreements with Salt River Project, Arizona Electric Power Cooperative & Western Area Power Administration in May 2017.

In conjunction with the Scheduling Entity Agreements, the Authority needed to review and approve the Dynamic Signaling Agreements. Although we were not party to the agreement, the Power Sales Contract required the Authority's approval before execution.

All of this was aided by having a full slate of Commissioners. Lawrence V. Robertson Jr. and John F. Sullivan were slated as Commissioners in March, 2017. Commissioner Robertson has spent 50+ years practicing law in energy, utilities and natural resources. Commissioner Sullivan has spent 40+ years with Salt River Project both in power and water, retiring as Deputy General Manager.

With the addition of two new Commissioners, and multiple requests from customers, a decision was made to revisit the results of the Strategic Planning Session. The first step in the process was that we conducted a customer survey, examining the Strategic Planning Session results and evaluating the Authority as a whole. The results were quite eye-opening and precipitated an update to the strategic vision.



The Strategic Vision that resulted called for;

Be a Leader for Hoover, Arizona, the Colorado River and Public Power as a Whole

Strive for Operational Excellence

Create and Sustain a Culture of Customer Service

Entertain Smart Opportunities

While the Authority has focused on Hoover operations for decades, the role of the Authority has been broadened to include more involvement in Colorado River and Public Power issues in general. To get there, we need a strong team and a deep bench. Therefore, the Authority has implemented monthly staff development trainings and quarterly trainings that are open to customers and legislators.



These quarterly trainings are just one aspect of the formal customer service program that we have implemented. We will explore this program and more in the subsequent sections, but I can't sign off without highlighting the incredible work of the staff over the last few years.

In June of 2017, Moody's upgraded our rating to Aa1, a rating that is only held by four other Public Power entities. This upgrade was due in part to all of the time and effort that staff at the Arizona Power Authority has put in over the last few years. Held by only four other public power entities, this rating by Moody's is a significant accomplishment. This recognition speaks to the dedication of the Commissioners and staff at the Arizona Power Authority, and I look forward to continued progress in the years to come.

Ed Gerak

Executive Director

Good company in a journey makes the way seem shorter. -Izaak Walton

Operations

The last low head turbine runner along with thrust bearing shoes and shift ring, N5, was installed in the spring of 2017. The multi-year generator life extension program is ongoing with inspections on units A1, A2, A7 and N3. The generators are approaching the end of their 30-40 year service life, and the assessment of generator equipment helps plan for scheduling and budgeting of generator maintenance and replacements.

Customer Service Report

In 2017 we implemented a Customer Service Program that includes regional customer visits, a quarterly Speaker Series, and monthly professional development training for APA Staff. We have worked hard to develop an active C^3 Customer Consultation Committee that meets regularly to discuss important issues. The APA has also planned two VIP Tours of Hoover Dam for the Legislators and their staff.

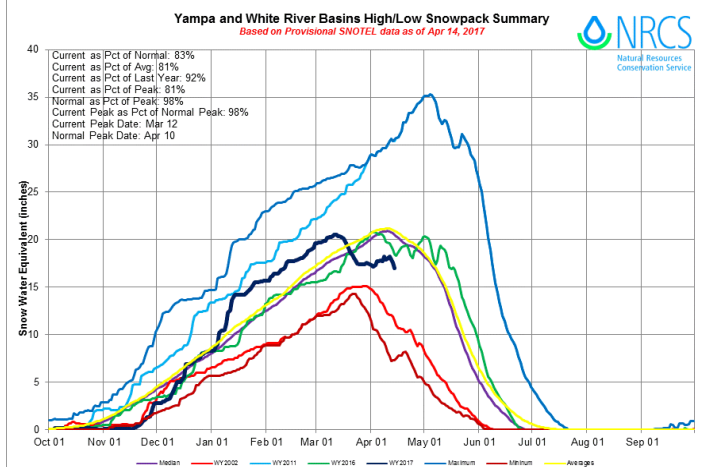
Staff developed a formal Customer Survey that brought to light areas in which additional efforts are needed with regard to customer service. The results of this survey were used to refine the Strategic Vision and Values that the APA has adopted and will guide the APA into the future.

Your customer doesn't care how much you know until they know how much you care.—Damon Richards.



Hydrology

Soil moisture in the fall of 2016 was predominantly dry in the lower basin and much of the upper basin, which resulted in less efficient runoff. Precipitation conditions during the fall were also below average, and when there was precipitation, it was usually rain. However, December brought snow as a result of much cooler and wetter conditions which continued through January. The season brought an “atmospheric river”, a narrow corridor of moisture through the basin area. Unfortunately by March, dry conditions returned, bringing melting snow and record runoff volumes.



Through the end of spring, northern areas of the basin were generally wetter while southern areas were drier. On the year, precipitation was 109% of average, with inflow to Lake Powell at 111% of average. Lake Mead elevation increased by over 5 feet during the operation year. Lake Powell's operations were governed by the Upper Elevation Balancing Tier, resulting in the release of 9 million acre feet of water to Lake Mead. Year-end conditions point to a dry winter for the coming operating year.

Management's Discussion & Analysis

The CliftonLarsonAllen Audited Financial Statements and Supplementary Information are attached for your review. Included in this attachment, beginning on page 3, is the Management's Discussion & Analysis. The information contained in the Management's Discussion and Analysis is intended to provide a general overview of the Authority's finances. Questions concerning any of the information provided in this report, or requests for additional financial information should be addressed to the Accounting Department:

Arizona Power Authority
c/o Accounting Department
1810 West Adams Street
Phoenix, AZ 85007



