

2023

COMBINED FINANCIAL STATEMENTS

TOGETHER WITH REPORT OF INDEPENDENT AUDITORS
AS OF APRIL 30, 2023 AND 2022



Delivering water and power®



COMBINED FINANCIAL STATEMENTS FOREWORD/DISCLAIMER

SRP is a community-based not-for-profit water and energy company that serves more than 2 million people in central Arizona. In keeping with our commitment to transparency, attached are the 2023 Combined Financial Statements together with the Report of Independent Auditors. Questions or comments about this document should be addressed to Brian J. Koch, Treasurer & Senior Director, Financial Services, at **(602) 236-2993**.

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Report of Independent Auditors

To Management, the Board of Directors of Salt River Project Agricultural Improvement and Power District and the Board of Governors of Salt River Valley Water Users' Association

Opinion

We have audited the accompanying combined financial statements of Salt River Project Agricultural Improvement and Power District and its subsidiaries and the Salt River Valley Water Users' Association (the "Company"), which comprise the combined balance sheets as of April 30, 2023 and 2022, and the related combined statements of net revenues and of cash flows for the years then ended, including the related notes (collectively referred to as the "combined financial statements").

In our opinion, the accompanying combined financial statements present fairly, in all material respects, the financial position of the Company as of April 30, 2023 and 2022, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (US GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Combined Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of the combined financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of combined financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the combined financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for one year after the date the combined financial statements are available to be issued.

Auditors' Responsibilities for the Audit of the Combined Financial Statements

Our objectives are to obtain reasonable assurance about whether the combined financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with US GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the combined financial statements.



In performing an audit in accordance with US GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the combined financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the combined financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the combined financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

PricewaterhouseCoopers LLP

June 30, 2023

**SALT RIVER PROJECT
COMBINED BALANCE SHEETS
APRIL 30, 2023 AND 2022
(Thousands)**

	<u>ASSETS</u>	<u>2023</u>	<u>2022</u>
Utility Plant			
Plant in Service-			
Electric		\$ 16,683,057	\$ 15,938,260
Irrigation		596,210	575,630
Common		1,342,623	1,340,145
Total plant in service		18,621,890	17,854,035
Less – accumulated depreciation on plant in service		(10,180,268)	(9,604,689)
		8,441,622	8,249,346
Plant held for future use		45,270	45,270
Construction work in progress		770,196	651,204
Nuclear fuel, net		142,101	128,085
		9,399,189	9,073,905
Other Property and Investments			
Non-utility property and other investments		391,218	559,808
Segregated funds, net of current portion		1,844,276	1,770,435
		2,235,494	2,330,243
Current Assets			
Cash and cash equivalents		295,945	486,702
Temporary investments		276,245	221,898
Current portion, segregated funds		104,746	99,177
Receivables, net of allowance for doubtful accounts of \$5,847 and \$5,494, respectively		315,526	290,017
Fuel stocks		110,041	90,068
Materials and supplies		330,204	279,253
Current commodity derivative assets		-	87,945
Other current assets		45,289	42,303
		1,477,996	1,597,363
Deferred Charges and Other Assets			
Regulatory assets		587,937	678,115
Non-current commodity derivative assets		37,016	39,209
Other deferred charges and other assets		196,625	217,705
		821,578	935,029
Total Assets		\$ 13,934,257	\$ 13,936,540

The accompanying notes are an integral part of these combined financial statements.

**SALT RIVER PROJECT
COMBINED BALANCE SHEETS
APRIL 30, 2023 AND 2022
(Thousands)**

CAPITALIZATION AND LIABILITIES

	<u>2023</u>	<u>2022</u>
Long-term Debt	\$ 4,950,900	\$ 4,560,487
Accumulated Net Revenues	<u>6,002,590</u>	<u>6,364,120</u>
Total Capitalization	<u>10,953,490</u>	<u>10,924,607</u>
Current Liabilities		
Current portion of long-term debt	113,930	108,910
Accounts payable	318,553	261,036
Accrued taxes and tax equivalents	121,995	129,214
Accrued interest	67,603	62,915
Customers' deposits	139,589	127,463
Current commodity derivative liabilities	98,668	9,049
Other current liabilities	<u>261,037</u>	<u>288,637</u>
	<u>1,121,375</u>	<u>987,224</u>
Deferred Credits and Other Non-current Liabilities		
Accrued post-retirement liability	713,636	848,684
Asset retirement obligations	377,324	372,802
Non-current commodity derivative liabilities	9,427	13,292
Other deferred credits and other non-current liabilities	<u>759,005</u>	<u>789,931</u>
	<u>1,859,392</u>	<u>2,024,709</u>
Commitments and Contingencies (Notes 9, 10, 11, 12, 13, 14, 15 and 16)		
Total Capitalization and Liabilities	<u>\$ 13,934,257</u>	<u>\$ 13,936,540</u>

The accompanying notes are an integral part of these combined financial statements.

SALT RIVER PROJECT
COMBINED STATEMENTS OF NET REVENUES
FOR THE YEARS ENDED APRIL 30, 2023 AND 2022
(Thousands)

	2023	2022
Operating Revenues		
Retail electric	\$ 3,211,366	\$ 2,993,392
Other electric	86,526	83,165
Wholesale	699,635	462,979
Water	24,019	25,805
Total operating revenues	4,021,546	3,565,341
Operating Expenses		
Power purchased	704,023	701,451
Fuel used in electric generation	1,537,262	284,092
Operations and maintenance	1,236,743	1,169,058
Depreciation and amortization	670,091	645,895
Taxes and tax equivalents	165,514	177,971
Total operating expenses	4,313,633	2,978,467
Net operating (expenses) revenues	(292,087)	586,874
Other (Expense) Income		
Investment income (loss), net	30,762	(68,631)
Other income, net	31,650	7,002
Total other income (expense), net	62,412	(61,629)
Net (expenses) revenues before financing costs	(229,675)	525,245
Financing Costs		
Interest on bonds, net	178,369	181,756
Capitalized interest	(14,402)	(12,298)
Amortization of bond discount (premium) and issuance expenses	(46,090)	(41,486)
Interest on other obligations	13,978	2,666
Net financing costs	131,855	130,638
Net (Expenses) Revenues	\$ (361,530)	\$ 394,607

The accompanying notes are an integral part of these combined financial statements.

SALT RIVER PROJECT
COMBINED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED APRIL 30, 2023 AND 2022
(Thousands)

	2023	2022
Cash Flows from Operating Activities		
Net (Expenses) Revenues	\$ (361,530)	\$ 394,607
Adjustments to reconcile net revenues to net cash provided by operating activities:		
Depreciation and amortization	670,091	645,895
Amortization of nuclear fuel	39,028	39,166
Amortization of bond discount (premium) and issuance expenses	(46,090)	(41,486)
Amortization of operating lease right of use assets	9,393	9,382
Change in fair value of derivative instruments, net of collateral	175,892	(188,383)
Change in fair value of investment securities	23,120	124,641
Realized gain on investing activities	(15,267)	(35,265)
Other	(2,920)	3,148
Decrease (increase) in:		
Fuel stocks and materials and supplies	(70,924)	24,948
Receivables, net of allowance for doubtful accounts	(29,825)	8,562
Other current assets	(2,986)	(2,554)
Deferred charges and other assets	4,620	(20,123)
Increase (decrease) in:		
Accounts payable	51,736	31,994
Accrued taxes and tax equivalents	(7,219)	5,890
Accrued interest	4,688	(309)
Customers' deposits and other current liabilities	(16,688)	33,279
Deferred credits and other non-current liabilities	(62,397)	4,575
Net cash provided by operating activities	362,722	1,037,967
Cash Flows from Investing Activities		
Capital expenditures	(1,311,014)	(1,014,150)
Plant acquisition	(34,979)	(46,891)
Contributions in aid of construction	313,912	226,794
Proceeds from disposition of assets	11,577	17,132
Purchases of investments	(216,908)	(478,929)
Sales of investments	70,287	60,575
Maturities of investments	231,896	291,066
Other investing activities	-	(1,191)
Net cash used for investing activities	(935,229)	(945,594)
Cash Flows from Financing Activities		
Proceeds from issuance of Revenue Bonds, net of debt issuance costs	554,716	653
Contribution to Revenue Bonds refunding	-	(6,955)
Repayment of Revenue Bonds	(108,910)	(102,755)
Repayment of Revolving Credit Agreement loan	(3,500)	-
Net cash provided by (used for) financing activities	442,306	(109,057)
Net (Decrease) Increase in Cash, Cash Equivalents and Restricted Cash	(130,201)	(16,684)
Balance at Beginning of Year in Cash, Cash Equivalents and Restricted Cash	612,670	629,354
Balance at End of Year in Cash, Cash Equivalents and Restricted Cash	\$ 482,469	\$ 612,670
Supplemental Information		
Cash paid for interest, net of capitalized interest	\$ 173,257	\$ 172,433

The accompanying notes are an integral part of these combined financial statements.

SALT RIVER PROJECT
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2023 AND 2022

(1) BASIS OF PRESENTATION:

The Company

The Salt River Project Agricultural Improvement and Power District (the District) is an agricultural improvement district organized in 1937 under the laws of the State of Arizona. It operates the Salt River Project (the Project), a federal reclamation project, under contracts with the Salt River Valley Water Users' Association (the Association), by which it has assumed the obligations and assets of the Association, including its obligations to the United States of America for the care, operation and maintenance of the Project. The District owns and operates an electric system that generates, purchases, transmits and distributes electric power and energy, and provides electric service to residential, commercial, industrial and agricultural power users in a 2,900-square-mile service territory in parts of Maricopa, Gila and Pinal counties, plus mine loads in an adjacent 2,400-square-mile area in Gila and Pinal counties. The Association, incorporated under the laws of the Territory of Arizona in 1903, operates an irrigation system as the agent of the District. The District and the Association are together referred to as Salt River Project or SRP.

Principles of Combination

The accompanying Combined Financial Statements reflect the combined accounts of the Association and the District. The District's financial statements are consolidated with its wholly owned taxable subsidiaries: SRP Captive Risk Solutions, Limited (CRS), Papago Park Center, Inc. (PPC), New West Energy Corporation (New West Energy), and Horizon Acquisitions LLC (Horizon). CRS is a domestic captive insurer, incorporated and domiciled in Arizona, which is utilized to enhance the District's property and casualty insurance programs. PPC is a real estate management company. New West Energy was used to market, at retail, energy available to the District that was surplus to the needs of its retail customers and energy that might have been rendered surplus in Arizona by retail competition in the supply of generation but is now largely inactive. Horizon is a land acquisition company. Net revenues, assets and liabilities related to the District's wholly owned taxable subsidiaries' operations are not material to the accompanying Combined Financial Statements. All intercompany transactions and balances have been eliminated.

Possession and Use of Utility Plant

The United States of America retains a paramount right or claim in the Project that arises from the original construction and operation of certain of the Project's electric and water facilities as a federal reclamation project. Rights to the possession and use of, and to all revenues produced by, these facilities are evidenced by contractual arrangements with the United States of America. The Department of Interior has the right to perform audits of certain of the operations of the Project. In addition, the District seeks approval from the Department of Interior for certain transactions such as payments of in-lieu taxes. The District also gives the Department of Interior the opportunity to raise any objections it may have regarding the issuance of revenue bonds.

Basis of Accounting

The accompanying Combined Financial Statements are presented in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). The preparation of financial statements in compliance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts in the financial statements and disclosures of contingencies. Actual results could differ from the estimates.

By virtue of SRP operating a federal reclamation project under contract, with the federal government’s paramount rights, asset ownership and certain approval rights, SRP is subject to accounting standards as set forth by the Federal Accounting Standards Advisory Board (FASAB). Entities reporting in accordance with the standards issued by the Financial Accounting Standards Board (FASB) prior to October 19, 1999 (the date the American Institute of Certified Public Accountants designated the FASAB as the accounting standard-setting body for entities under the federal government), are permitted to continue to report in accordance with those standards. As permitted, SRP has elected to report its financial statements in accordance with FASB standards.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Utility Plant

Utility plant is stated at the historical cost of construction. Capitalized construction costs include labor, materials, services purchased under contract, and allocations of indirect charges for engineering, supervision, transportation and administrative expenses and an allowance for funds used during construction (AFUDC). The cost of property that is replaced, removed or abandoned, less salvage, is charged to accumulated depreciation. Repairs and maintenance costs are charged to operations and maintenance expense.

Depreciation expense is computed on a straight-line basis over recovery periods of the various classes of plant assets. Depreciation expense for utility plant totaled \$663.8 million and \$637.5 million for the fiscal years ended April 30, 2023 and 2022, respectively. The following table reflects the District’s average depreciation rates on the average cost of depreciable assets for the fiscal years ended April 30:

	<u>2023</u>	<u>2022</u>
Average electric depreciation rate	3.32%	3.28%
Average irrigation depreciation rate	2.15%	2.25%
Average common depreciation rate	6.33%	6.49%

There was an increase of \$5.0 million and \$39.2 million in property, plant and equipment purchases within accounts payable for the fiscal years ended April 30, 2023 and 2022, respectively. Such changes are considered a non-cash investing activity.

Plant Held for Future Use

Plant held for future use primarily includes the cost of land acquired for future operations, including generation, transmission and other purposes. Once development starts on the new facility, the costs will be moved to plant in service.

Allowance for Funds Used During Construction

AFUDC is the estimated cost of funds used to finance plant additions and is recovered in prices through depreciation expense over the useful life of the related asset. AFUDC is capitalized during certain plant construction and is included in capitalized interest in the accompanying Combined Statements of Net Revenues. Composite rates of 3.10% and 3.15% were applied in fiscal years 2023 and 2022, respectively, to calculate interest on funds used to finance construction work in progress, resulting in \$14.4 million and \$12.3 million of interest capitalized, respectively.

Nuclear Fuel

SRP amortizes the cost of nuclear fuel using the units-of-production method. The units-of-production method is an amortization method based on actual physical usage. The nuclear fuel amortization and accrued expenses for

both the interim and permanent disposal of spent nuclear fuel are components of fuel expense. Nuclear fuel amortization was \$39.0 million and \$39.2 million in fiscal years 2023 and 2022, respectively. The balance of nuclear fuel includes \$114.8 million and \$84.6 million of in-process stock, which is not yet being amortized, as of April 30, 2023 and 2022, respectively.

Software Costs

SRP capitalizes costs incurred to purchase and develop internal-use computer software and implementation costs incurred in a cloud computing arrangement that is a service contract and amortizes such costs over the recovery periods of the products. Capitalized software costs are included in utility plant and cloud computing costs are included in other deferred charges and other assets in the accompanying Combined Balance Sheets. The following table summarizes the capitalized computer software and capitalized cloud computing arrangement implementation costs as of April 30 (in thousands):

	2023		2022	
	Software	Cloud Computing	Software	Cloud Computing
Asset balance	\$ 723,991	\$ 39,029	\$ 708,477	\$ 38,638
Accumulated amortization	571,925	9,043	538,387	4,737

For the fiscal years ended April 30, 2023 and 2022, amortization expense for capitalized software costs was \$33.5 million and \$36.3 million, respectively. Amortization expense for capitalized cloud computing arrangements implementation costs was \$4.3 million and \$3.6 million for the fiscal years ended April 30, 2023 and 2022, respectively.

The following table presents estimated future amortization expense pertaining to capitalized software costs and capitalized cloud computing arrangement implementation costs in fiscal years ending April 30 (in thousands):

	Software	Cloud Computing
2024	\$ 32,005	\$ 4,142
2025	31,278	3,771
2026	27,384	3,587
2027	21,614	3,555
2028	18,174	3,524

Asset Retirement Obligations

SRP accounts for its asset retirement obligations in accordance with authoritative guidance, which requires the recognition and measurement of liabilities for legal obligations associated with the retirement of tangible long-lived assets. Liabilities for asset retirement obligations are recognized at fair value as incurred and capitalized as part of the cost of the related tangible long-lived assets. Accretion of the liabilities, due to the passage of time, is an operating expense and the capitalized cost is depreciated over the estimated useful life of the long-lived asset. Retirement obligations associated with long-lived assets are those for which a legal obligation exists under enacted laws, statutes and contracts, including obligations arising under the doctrine of promissory estoppel.

The District has identified retirement obligations for its share of Palo Verde Nuclear Generating Station (PVNGS), Navajo Generating Station (NGS), Four Corners Generating Station (Four Corners), and certain other assets. Amounts recorded for asset retirement obligations are subject to various assumptions and determinations, such as determining whether an obligation exists to remove assets, estimating the fair value of the costs of removal,

estimating when final removal will occur and determining the credit-adjusted, risk-free interest rates to be utilized in discounting future liabilities. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the asset retirement obligation (with corresponding adjustments to utility plant), which can occur due to a number of factors, including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in federal, state and local regulations and changes to the estimated decommissioning date of the assets, as well as for the accretion of the liability due to the passage of time until the obligation is settled.

The following table summarizes the asset retirement obligation activity of the District as of and for the fiscal years ended April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Beginning balance, May 1	\$ 372,802	\$ 364,459
Additions	-	4,350
Settlements, net	(10,641)	(10,362)
Revisions to estimates	61	(201)
Accretion expense	15,102	14,556
Ending balance, April 30	<u>\$ 377,324</u>	<u>\$ 372,802</u>

Investments in Debt and Equity Securities

SRP invests in various debt and equity securities. Debt securities in which SRP has the intent and ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost. Debt securities that are bought and held with the likelihood of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in investment income, net. SRP has adopted the fair value option for all debt and equity securities other than debt securities classified as held-to-maturity. All such securities are reported at fair value, with unrealized gains and losses included in investment (loss) income, net, with the exception of the Nuclear Decommissioning Trust (NDT) for which unrealized gains and losses are recorded in regulatory liabilities (see table in Segregated Funds). SRP does not classify any securities as available-for-sale.

Temporary Investments

Debt and equity securities that are short-term in nature and are expected to be sold or converted to cash in the next twelve months are classified as temporary investments on the Combined Balance Sheets, unless they meet the definition of a cash equivalent.

Segregated Funds

The District sets aside funds that are segregated due to management intent and to support various purposes. The District also has certain segregated funds that are legally restricted. The following amounts are included in segregated funds in the accompanying Combined Balance Sheets as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Segregated funds – legally restricted		
Nuclear Decommissioning Trust	\$ 576,441	\$ 571,676
Debt Reserve Fund	80,598	80,598
Construction Fund	57,322	-
Other	35,851	36,343
Total segregated funds – legally restricted	<u>750,212</u>	<u>688,617</u>
Segregated funds – other		
Benefits funds	1,093,253	1,081,218
Debt Service Fund	104,746	99,177
Other	811	600
Total segregated funds – other	<u>1,198,810</u>	<u>1,180,995</u>
Total segregated funds, including current portion	<u>\$ 1,949,022</u>	<u>\$ 1,869,612</u>

Nuclear Decommissioning

In accordance with regulations of the Nuclear Regulatory Commission, the District maintains a trust for the decommissioning of PVNGS. The NDT funds are invested in debt and equity securities. All NDT debt securities are reported as trading securities. SRP has elected the fair value option for such securities. Changes in fair value related to the NDT securities are included in the nuclear decommissioning regulatory liability with no impact to net revenues. The NDT funds are classified as segregated funds in the accompanying Combined Balance Sheets.

Cash and Cash Equivalents

Cash equivalents include money market funds and highly liquid short-term investments with original maturities of three months or less.

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the Combined Balance Sheets and the Combined Statements of Cash Flows as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Cash and cash equivalents	\$ 295,945	\$ 486,702
Cash and cash equivalents included in non-utility property and other investments	21,928	21,953
Cash and cash equivalents included in segregated funds	104,147	98,799
Restricted cash and cash equivalents included in segregated funds	60,449	5,216
Total cash, cash equivalents and restricted cash	<u>\$ 482,469</u>	<u>\$ 612,670</u>

Amounts included in restricted cash represent those required to be set aside per terms of contractual agreements, bond indentures or other legal stipulations.

Allowance for Doubtful Accounts

Allowance for doubtful accounts is provided for electric customer accounts and other non-energy receivables balances based upon the current expected credit loss, which is measured using a historical experience rate of write-offs, adjusted for economic factors that include expected recoveries, the current economic environment,

pertinent market studies, and observed customer behavior. The allowance is adjusted periodically for this experience rate and is maintained until either receipt of payment or the likelihood of collection is considered remote, at which time the allowance and the corresponding receivable balance are written off.

The following table summarizes SRP's changes in allowance for doubtful accounts for the fiscal years ended April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Beginning balance, May 1	\$ 5,494	\$ 6,013
Provision for doubtful accounts	4,688	8,669
Write-offs	(4,335)	(9,188)
Ending balance, April 30	<u>\$ 5,847</u>	<u>\$ 5,494</u>

Fuel Stocks and Materials and Supplies

Fuel stocks and materials and supplies are stated at weighted-average cost and are valued using the average cost method.

Other Current Liabilities

The accompanying Combined Balance Sheets include the following other current liabilities as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Sick, vacation and holiday accrual	\$ 55,103	\$ 53,202
Customer prepayments	56,154	75,908
Employee Performance Incentive Compensation (EPIC)	30,697	34,438
Post-retirement benefits	33,382	33,673
Other	85,701	91,416
Total other current liabilities	<u>\$ 261,037</u>	<u>\$ 288,637</u>

Other Deferred Credits and Non-current Liabilities

The accompanying Combined Balance Sheets include the following other deferred credits and non-current liabilities as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Regulatory liabilities	\$ 461,384	\$ 486,182
Sick, vacation and holiday accrual	54,952	56,899
Long-term operating lease liabilities	56,602	61,247
Mine reclamation and other environmental obligations	49,083	50,225
Other	136,984	135,378
Total other deferred credits and non-current liabilities	<u>\$ 759,005</u>	<u>\$ 789,931</u>

Financing Costs

Bond discount, premium and issuance expenses are deferred and amortized using the effective interest method over the terms of the related bond issues.

Income Taxes

The District, as a political subdivision of the State of Arizona, is exempt from federal and Arizona state income taxes. The Association, as a private corporation, is not exempt from federal and Arizona state income taxes. However, the Association is not liable for income taxes on operations relating to its acting as an agent for the District on the basis of a settlement with the Commissioner of Internal Revenue in 1949, which was approved by the Secretary of the Treasury. The Association is liable for income taxes on activities where it is not acting as an agent of the District. Income taxes related to the Association and to the District's wholly owned taxable subsidiaries' operations are not material to the accompanying Combined Financial Statements.

Voluntary Contributions in Lieu of Taxes

As a political subdivision of the State of Arizona, the District is exempt from property taxation. In accordance with Arizona law, the District makes voluntary contributions each year to the State of Arizona, school districts, cities, counties, towns and other political subdivisions of the State of Arizona, for which property taxes are levied and within whose boundaries the District has property included in its electric system. The amount paid is computed on the same basis as ad valorem taxes paid by a private utility corporation with an allowance for certain water-related deductions. Such contributions are included in taxes and tax equivalents in the Combined Statements of Net Revenues.

Sales and Use Taxes

The District is required by various government authorities, including states and municipalities, to collect and remit taxes on certain retail sales. Such taxes are recorded on a net basis and excluded from revenues and expenses in the accompanying Combined Financial Statements.

Concentrations of Credit Risk

Financial instruments that potentially subject SRP to credit risk consist of cash and cash equivalents, temporary and other investments, and segregated funds. Certain balances exceed Federal Deposit Insurance Corporation (FDIC) insured limits or are invested in money market accounts with investment banks that are not FDIC insured. SRP's cash and cash equivalents, temporary and other investments, and segregated funds are placed in creditworthy financial institutions and certain money market accounts that invest in U.S. Treasury securities or other obligations issued or guaranteed by the U.S. government or its agencies or instrumentalities.

The use of contractual arrangements to manage the risks associated with changes in energy commodity prices creates credit risks resulting from the possibility of nonperformance by counterparties pursuant to the terms of their contractual obligations. In addition, volatile energy prices can create significant credit exposure from energy market receivables and mark-to-market valuations. The District has a credit policy for wholesale counterparties, continuously monitors credit exposures and routinely assesses the financial strength of its counterparties. The District minimizes credit risk by dealing primarily with creditworthy counterparties, entering into standardized agreements that allow netting of exposures to and from a single counterparty, and requiring letters of credit, parent guarantees or other collateral when it does not consider the financial strength of the counterparty sufficient.

Subsequent Events

SRP follows authoritative guidance which requires an entity to evaluate subsequent events through the date that the financial statements are either issued or available to be issued. Subsequent events for SRP have been evaluated through June 30, 2023, which is the date that the financial statements were issued. See Note [16], SUBSEQUENT EVENTS for additional discussion of subsequent events.

(3) ACCOUNTING PRONOUNCEMENTS:

In March 2020, the FASB issued ASU 2020-04, *Reference Rate Reform*, as amended. The amendments in this update provide optional expedients and exceptions for applying U.S. GAAP to contracts that reference the London Interbank Offered Rate or another reference rate expected to be discontinued by reference rate reform. In December 2022, the FASB issued ASU 2022-06, which amended the dates when an entity may elect to apply this update to any time from March 12, 2020 through December 31, 2024. Once elected, the expedients must be applied prospectively for all eligible contracts. SRP has not identified any contracts that would be affected by this update. If any contracts are modified to replace a reference rate, SRP will elect the expedients provided by these updates.

(4) REGULATORY MATTERS:

The Electric Utility Industry

The District operates in a regulated environment in which it has an obligation to deliver electric service to customers within its service area. In 1998, Arizona legislature enacted the Arizona Electric Power Competition Act (the Act), which applies to public power entities like the District. The Act authorized competition in the retail sales of electric generation, recovery of stranded costs and competition in billing, metering and meter reading. While retail competition was available to all customers by 2001, only a few customers chose an alternative energy provider, and those customers have since returned to their incumbent utilities. At this time, there is no active retail competition within the District's service territory or, to the knowledge of the District, within the State of Arizona, and the District's Direct Access Program is suspended.

The Arizona Corporation Commission (ACC) regulates investor-owned and cooperatively owned utilities, called public service corporations in Arizona. The Arizona Legislature, in the Act, directed the ACC to adopt rules for competition similar to what the Arizona Legislature had enacted for public power entities. In 1999, the ACC issued its rules for retail electric competition. The rules were challenged in the courts and held to be invalid. At various times since, numerous energy service, meter reading and meter service providers, brokers, large industrial customers and merchant power plant owners have urged the ACC to reinstate some form of retail competition, but none have been successful.

In May 2013, the ACC opened an inquiry into retail competition and requested that interested parties provide comments on a series of ACC-issued questions. The District participated in that inquiry. On September 11, 2013, the ACC voted to close the inquiry into whether the ACC should consider deregulation of the Arizona electricity market. The ACC's action was consistent with the position advocated by the District but there was insufficient support to modify the rules of competition. However, effective July 1, 2012, the ACC approved a buy-through program for a major utility allowing a limited number of large industrial customers to purchase generation from other providers. In December 2020, the ACC approved a similar buy-through program for a second major utility in the state. The ACC continues to evaluate these programs as part of rate case proceedings.

In August 2021, an entity filed application to provide competitive electric generation services in Arizona under the 1998 law. This action led to discussions which resulted in the ACC requesting a legal opinion from the Arizona Attorney General. This resulted in an ACC directive stating that all matters be held in abeyance until a finding from the Attorney General. That opinion was not issued and there was a change in the Attorney General because of the 2022 election. At this time, there is no upcoming matter to modify the rules, but the District is actively monitoring the issue. In addition, during the 2022 legislative session, House Bill 2101 was enacted and has since become effective. House Bill 2101 repeals statutes and removes the requirement that a competitive market exist in the sale of electric generation service in Arizona. As part of the House Bill 2101 stakeholder process, the District negotiated an agreement that creates its own buy-through program. The terms and conditions of the program are

being established and the program is expected to go before the District Board in September for approval. If the District Board approves the program's structure, it will be implemented in January 2024.

Regulation and Pricing Policies

Under Arizona law, the District's publicly elected Board of Directors (the Board) has the authority to establish electric prices. The District is required to follow certain public notice and special Board meeting procedures before implementing any changes in the standard electric price plans. The financial statements reflect the pricing policies of the Board.

The District's price plans include a base price component and a Fuel and Purchased Power Adjustment Mechanism (FPPAM). Base prices recover costs for generation, transmission, distribution, customer services, metering, meter reading, billing and collections, and system benefits charges that are not otherwise recovered through the FPPAM. The FPPAM was implemented in May 2002 to adjust for increases and decreases in fuel costs and, as of May 1, 2019, also includes renewable purchased power agreements. Through a system benefits charge to the District's transmission and distribution customers, the District recovers the costs of programs benefiting the general public, such as discounted rates for low-income customers, energy efficiency and nuclear decommissioning, including the cost of spent fuel storage.

On September 12, 2022, the Board voted to approve two increases to FPPAM prices: the first overall 4.7% increase effective November 1, 2022, and the second increase of the same magnitude effective a year later, November 1, 2023. The Board also approved forgoing future collection of \$124.0 million of the under-collected FPPAM balance, using the District's strong financial position to reduce the need for price increases in the future. On March 28, 2023, the Board voted to approve an additional overall increase through FPPAM rates of 4.9% to the already approved increase of 4.7% effective November 1, 2023, for a total overall price increase of 9.6% compared to current price levels.

Regulatory Accounting

SRP accounts for the financial effects of the regulated portion of its operations in accordance with the provisions of authoritative guidance for regulated enterprises, which requires cost-based, rate-regulated utilities to reflect the impacts of regulatory decisions in their financial statements. SRP records regulatory assets, which represent probable future recovery of certain costs from customers through the pricing process, and regulatory liabilities which represent probable future credits to customers through the pricing process or current collections for future expected costs. Based on actions of the Board, SRP believes the future collection of costs deferred as regulatory assets is probable. If events were to occur making recovery of these regulatory assets no longer probable, SRP would be required to write off the remaining balance of such assets as a one-time charge to net revenues. None of the regulatory assets earn a return.

The accompanying Combined Balance Sheets include the following regulatory assets and liabilities as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Assets		
Pension and other post-retirement benefits (Note [12])	\$ 493,032	\$ 581,530
Bond defeasance	75,826	83,958
Other	19,079	12,627
Total regulatory assets	<u>\$ 587,937</u>	<u>\$ 678,115</u>
Liabilities		
Nuclear decommissioning	\$ 372,096	\$ 378,040
Depreciation	58,255	72,496
Bond defeasance	31,033	35,646
Total regulatory liabilities	<u>\$ 461,384</u>	<u>\$ 486,182</u>

The pension and other post-retirement benefits regulatory asset is adjusted as changes in actuarial gains and losses, prior service costs and transition assets or obligations are recognized as components of net periodic pension costs each fiscal year and is recovered through prices charged to customers.

Bond defeasance regulatory assets and liabilities are recovered over the remaining original amortization periods of the reacquired debt ending in various years through fiscal year 2039.

The nuclear decommissioning regulatory liability is any difference between current fiscal year costs and revenues associated with nuclear decommissioning and earnings (losses) on the NDT. Such amounts are deferred in accordance with authoritative guidance for regulated enterprises and have no impact to SRP's earnings.

The depreciation regulatory liability, which results from depreciation that is accelerated in excess of straight-line depreciation, is being refunded over the estimated remaining lives of the assets.

(5) REVENUES:

SRP generates revenues primarily from the sale and delivery of electricity to retail customers. Retail revenues, including unbilled amounts, are generally recognized over time based upon volumes delivered because the customer consumes the electricity as it is delivered. Retail revenues are typically based on prices subject to regulatory oversight and are billed and received monthly. Payment is generally due in the month following delivery. See Note [4], REGULATORY MATTERS, for discussion of SRP's regulation and pricing policies. The estimated retail revenue for electricity delivered but not yet billed, recognized in retail electric revenues and recorded as receivables, net, was \$131.5 million and \$118.1 million for the fiscal years ended and as of April 30, 2023 and 2022, respectively.

SRP generates wholesale revenues primarily from excess energy sales, which are recognized over time as the energy is delivered because the customer consumes the electricity as it is delivered. Payments for wholesale sales are generally due in the month following delivery.

Some wholesale contracts are accounted for as derivative instruments. Fair value adjustments for these contracts increased wholesale revenues by \$13.8 million and reduced wholesale revenue by \$1.3 million in fiscal years 2023 and 2022, respectively. See Note [7], DERIVATIVE INSTRUMENTS.

SRP generates transmission revenues by allowing other entities to use the District's transmission facilities to transmit power. Payment for transmission services is generally due monthly and revenues are recognized over

time because the customer consumes the transmission service as it is provided. Transmission revenues are included in other electric revenues.

SRP generates telecommunications revenues by allowing companies to use the District’s infrastructure to place antennas that are used to transmit communications signals. Payment for telecommunication services is generally due up front and revenues are recognized over time as the service is provided. Telecommunication revenues are included in other electric revenues.

SRP generates water revenues from delivering water to SRP water customers through annual charges, supplemental water charges and various other fees. Payment of water charges and fees is generally due up front annually and revenues are recognized over time as water is delivered.

The following table summarizes SRP’s sources of revenues for the fiscal years ended April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Electric		
Residential	\$ 1,770,474	\$ 1,646,994
Commercial	1,138,205	1,059,062
Other retail customers	<u>302,687</u>	<u>287,336</u>
Total retail electric revenues	3,211,366	2,993,392
Other electric	86,526	83,165
Wholesale	<u>699,635</u>	<u>462,979</u>
Total electric operating revenues	3,997,527	3,539,536
Water	<u>24,019</u>	<u>25,805</u>
Total operating revenues	<u>\$ 4,021,546</u>	<u>\$ 3,565,341</u>

Deferred revenue balances are included in other current liabilities and were \$97.8 million and \$110.0 million as of April 30, 2023 and 2022, respectively. The deferred revenues generally represent amounts paid by or receivable from customers for which the associated performance obligation has not yet been satisfied. Substantially all of the deferred revenue balances are expected to be recognized within one year. SRP’s other contract assets are not significant.

Contracts with remaining performance obligations include the supply and delivery of various electric and water products and services. Contracts with variable volumes and/or variable pricing are excluded from disclosure of remaining performance obligations because the related consideration under the contracts are variable at inception. Contract lengths vary from cancelable to multiyear.

SRP does not disclose the value of remaining performance obligations when (1) the performance obligation is part of a contract that has an original expected duration of one year or less, (2) revenue is recognized from the satisfaction of the performance obligation in accordance with the “right to invoice” practical expedient, or (3) the consideration is allocated entirely to a wholly unsatisfied performance obligation or to a wholly unsatisfied promise to transfer a distinct good or service that forms part of a series of distinct goods or services. After applying these exemptions, SRP’s contracts with customers have no material remaining performance obligations.

(6) FAIR VALUE OF FINANCIAL INSTRUMENTS:

SRP invests in U.S. government obligations, certificates of deposit and other marketable investments. Such investments are classified as cash and cash equivalents, temporary investments, other investments and segregated funds in the accompanying Combined Balance Sheets depending on the purpose and duration of the investment.

Fair Value Option

SRP adopted authoritative guidance which permits an entity to measure many financial instruments and certain other items at fair value. SRP has elected the fair value option for all investment securities other than debt securities classified as held-to-maturity. Election of the fair value option for debt securities requires the security to be reported as a trading security.

The fair value option was elected because management believes that fair value best represents the nature of the investments. While the investment securities held in these funds are reported as trading securities, the investments continue to be managed with a long-term focus. Accordingly, all purchases and sales within these funds are presented separately in the accompanying Combined Statements of Cash Flows as investing cash flows, consistent with the nature and purpose for which the securities are acquired.

Realized and unrealized gains and losses on these investments are included in investment income, net, in the accompanying Combined Statements of Net Revenues.

The following table summarizes line items included in the accompanying Combined Balance Sheets as of April 30 that include amounts recorded at fair value pursuant to the fair value option (in thousands):

	Measurement Attribute	2023	2022
Cash and cash equivalents			
Cash*	N/A	\$ 10,945	\$ 12,702
Money market funds	Fair value	285,000	474,000
Held-to-maturity commercial paper	Amortized cost	-	-
Total cash and cash equivalents		<u>\$ 295,945</u>	<u>\$ 486,702</u>
Non-utility property and other investments			
Money market funds	Fair value	\$ 21,928	\$ 21,953
Equity investments	Fair value	57,938	58,973
Held-to-maturity debt investments	Amortized cost	136,880	312,812
Non-utility property*	N/A	174,472	166,070
Total non-utility property and other investments		<u>\$ 391,218</u>	<u>\$ 559,808</u>
Segregated funds, net of current portion			
Money market funds	Fair value	\$ 59,850	\$ 4,837
Equity investments	Fair value	1,695,124	1,678,522
Trading debt investments	Fair value	9,524	9,293
Held-to-maturity debt investments	Amortized cost	79,778	77,783
Total segregated funds, net of current portion		<u>\$ 1,844,276</u>	<u>\$ 1,770,435</u>
Temporary investments			
Held-to-maturity debt investments	Amortized cost	\$ 276,245	\$ 221,898
Total temporary investments		<u>\$ 276,245</u>	<u>\$ 221,898</u>
Current portion of segregated funds			
Money market funds	Fair value	\$ 104,746	\$ 99,177
Total current portion of segregated funds		<u>\$ 104,746</u>	<u>\$ 99,177</u>

*Asset category not eligible for fair value option

SRP's investments in debt securities are measured and reported at amortized cost when there is intent and ability to hold the security to maturity. SRP's amortized cost and fair value of held-to-maturity debt securities were \$492.9 million and \$469.1 million, respectively, as of April 30, 2023 and \$612.5 million and \$591.2 million,

respectively, as of April 30, 2022. As of April 30, 2023, SRP’s investments in debt securities have maturity dates ranging from May 2023 to February 2036.

As of April 30, 2023, the gross unrecognized holding gains and losses on held-to-maturity debt securities were approximately \$26.1 thousand and \$23.2 million, respectively.

SRP’s equity investments and trading debt investments are measured at fair value with unrealized gains and losses included in investment income, net. Unrealized gains and losses on NDT investments are included in the nuclear decommissioning regulatory liability.

The following table summarizes unrealized gains (losses) recognized during the fiscal year ending April 30 on trading securities still held as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Non-utility property and other investments	\$ (1,732)	\$ (7,625)
Segregated funds, net of current portion	(36,521)	(180,650)
Total	<u>\$ (38,253)</u>	<u>\$ (188,275)</u>

(7) DERIVATIVE INSTRUMENTS:

Energy Risk Management Activities

The District has an energy risk management program to limit exposure to risks inherent in normal energy business operations. The goal of the energy risk management program is to measure and manage exposure to market risks, credit risks and operational risks. Specific goals of the energy risk management program include reducing the impact of market fluctuations on energy commodity prices associated with customer energy requirements, reducing excess generation and fuel expenses, meeting customer pricing needs and maximizing the value of physical generating assets. The District employs established policies and procedures to meet the goals of the energy risk management program using various physical and financial instruments, including forward contracts, futures, swaps and options.

Certain of these transactions are accounted for as commodity derivatives and are recorded in the accompanying Combined Balance Sheets as either an asset or liability measured at their fair value. Derivative instruments and the related collateral accounts, if applicable, that are subject to master netting agreements are presented as a net asset or liability in the accompanying Combined Balance Sheets. Changes in the fair value of commodity derivatives are recognized each period in net operating revenues and included in the accompanying Combined Statements of Net Revenues and classified as part of operating cash flows in the accompanying Combined Statements of Cash Flows. Some of the District’s contractual agreements qualify and are designated for the normal purchases and normal sales exception and are not recorded at fair value in the accompanying Combined Balance Sheets. This exception applies to physical sales and purchases of power or fuel when it is probable that physical delivery will occur; the pricing provisions are clearly and closely related to the underlying asset; and the documentation requirements are met. If a contract qualifies for the normal purchases and normal sales scope exception, the District accounts for the contract using settlement accounting (costs and revenues are recorded when physical delivery occurs). SRP has not elected to use hedge accounting for its derivative instruments.

See Note [8], FAIR VALUE MEASUREMENTS, for additional information on derivative valuation.

Derivative Volumes

The District has the following gross derivative volumes, by type, as of April 30, 2023:

<u>Commodity</u>	<u>Unit of Measure</u>	<u>Sales Volumes</u>	<u>Purchases Volumes</u>
Natural gas options, swaps and forward arrangements	MMBtu	8,040,000	341,010,000
Electricity options, swaps and forward arrangements	MWh	624,475	99,000
Liquefied fuel swaps	Gallon	-	5,328,200

The District has the following gross derivative volumes, by type, as of April 30, 2022:

<u>Commodity</u>	<u>Unit of Measure</u>	<u>Sales Volumes</u>	<u>Purchases Volumes</u>
Natural gas options, swaps and forward arrangements	MMBtu	-	354,580,000
Electricity options, swaps and forward arrangements	MWh	905,525	-
Liquefied fuel swaps	Gallon	-	6,037,400

Presentation of Derivative Instruments in the Financial Statements

The following tables provide information about the gross fair values, netting, and collateral and margin deposits for derivative hedging instruments in the accompanying Combined Balance Sheets as of April 30 (in thousands):

	<u>2023</u>				
	<u>Current Commodity Derivative Assets</u>	<u>Non-current Commodity Derivative Assets</u>	<u>Current Commodity Derivative Liabilities</u>	<u>Non-current Commodity Derivative Liabilities</u>	<u>Net Assets (Liabilities)</u>
Commodities	\$ 6,465	\$ 85,138	\$ (111,377)	\$ (37,949)	\$ (57,723)
Netting	(6,465)	(28,522)	6,465	28,522	-
Collateral and margin deposits	-	(19,600)	6,244	-	(13,356)
Total	<u>\$ -</u>	<u>\$ 37,016</u>	<u>\$ (98,668)</u>	<u>\$ (9,427)</u>	<u>\$ (71,079)</u>

	<u>2022</u>				
	<u>Current Commodity Derivative Assets</u>	<u>Non-current Commodity Derivative Assets</u>	<u>Current Commodity Derivative Liabilities</u>	<u>Non-current Commodity Derivative Liabilities</u>	<u>Net Assets (Liabilities)</u>
Commodities	\$ 302,846	\$ 103,625	\$ (15,464)	\$ (25,231)	\$ 365,776
Netting	(6,278)	(11,939)	6,278	11,939	-
Collateral and margin deposits	(208,623)	(52,477)	137	-	(260,963)
Total	<u>\$ 87,945</u>	<u>\$ 39,209</u>	<u>\$ (9,049)</u>	<u>\$ (13,292)</u>	<u>\$ 104,813</u>

The following tables summarize the District’s unrealized gains (losses) associated with derivatives not designated as hedging instruments in the accompanying Combined Statements of Net Revenues for the fiscal year (in thousands):

<u>2023</u>				
	<u>Operating Revenues</u>	<u>Power Purchased</u>	<u>Fuel Used in Electric Generation</u>	<u>Change in Unrealized Gain (Loss)</u>
Commodities	\$ 13,801	\$ (500)	\$ (427,100)	\$ (413,799)

<u>2022</u>				
	<u>Operating Revenues</u>	<u>Power Purchased</u>	<u>Fuel Used in Electric Generation</u>	<u>Change in Unrealized Gain (Loss)</u>
Commodities	\$ (1,335)	\$ (1,034)	\$ 456,313	\$ 453,944

Credit-related Contingent Features

Certain of the District’s derivative instruments contain provisions that require the District to post additional collateral upon certain credit events. If the District’s debt were to fall below investment grade, the counterparties to the derivative instruments could demand immediate and ongoing full overnight collateralization on derivative instruments in net liability positions.

The aggregate fair value of all derivative liabilities with credit-risk-related contingent features as of April 30, 2023, was \$86.3 million. As of April 30, 2023, the District posted collateral in the amount of \$6.2 million as credit support under energy contracts for which the collateralization threshold was exceeded. If the credit-risk-related contingent features underlying these agreements were triggered on April 30, 2023, the District could be required to post up to \$80.1 million of additional collateral to its counterparties.

(8) FAIR VALUE MEASUREMENTS:

SRP accounts for fair value in accordance with authoritative guidance, which defines fair value, establishes methods for measuring fair value by applying one of three observable market techniques (market approach, income approach or cost approach) and establishes required disclosures about fair value measurements. This guidance defines fair value as the price that would be received for an asset or paid to transfer a liability, in the most advantageous market for the asset or liability in an arms-length transaction between willing market participants at the measurement date. SRP determines fair value of most of its financial instruments based on the market approach, which is defined as a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. Certain derivative positions are valued using the income approach, which derives fair value from estimated future cash flows, risk-adjusted discount rates and other inputs.

SRP classifies its financial instruments into the fair value hierarchy based on the inputs used to determine fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are as follows:

Level 1: Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market.

Level 2: Financial assets and liabilities whose values are based on quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in non-active markets,

pricing models whose inputs are observable for substantially the full term of the assets or liabilities and pricing models whose inputs are derived principally from or corroborated by observable market data through correlation or other means.

Level 3: Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management's own assumptions about the assumptions a market participant would use in pricing the asset or liability.

Assets measured at fair value using net asset value (NAV) as a practical expedient are not categorized in the fair value hierarchy. These assets are listed in the column "Other" in the following tables to permit the reconciliation to amounts presented in the financial statements.

The following table sets forth, by level within the fair value hierarchy, SRP's financial assets and liabilities that were accounted for at fair value on a recurring basis as of April 30, 2023 (in thousands):

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Other</u>	<u>Netting and Collateral</u>	<u>Total</u>
Assets						
Cash and cash equivalents:						
Money market funds	\$ -	\$ 285,000	\$ -	\$ -	\$ -	\$ 285,000
Total cash and cash equivalents	-	285,000	-	-	-	285,000
Non-utility property and other investments:						
Money market funds	-	21,928	-	-	-	21,928
Mutual funds	57,938	-	-	-	-	57,938
Total non-utility property and other investments	57,938	21,928	-	-	-	79,866
Segregated funds, net of current portion:						
Money market funds	-	59,850	-	-	-	59,850
Mutual funds	1,409,072	-	-	-	-	1,409,072
Commingled funds	-	-	-	286,052	-	286,052
Government securities	-	9,524	-	-	-	9,524
Total segregated funds, net of current portion	1,409,072	69,374	-	286,052	-	1,764,498
Current portion of segregated funds:						
Money market funds	-	104,746	-	-	-	104,746
Total current portion of segregated funds	-	104,746	-	-	-	104,746
Derivative instruments:						
Commodities	180	91,423	-	-	(54,587)	37,016
Total derivative instruments	180	91,423	-	-	(54,587)	37,016
Total assets	<u>\$1,467,190</u>	<u>\$ 572,471</u>	<u>\$ -</u>	<u>\$ 286,052</u>	<u>\$ (54,587)</u>	<u>\$2,271,126</u>
Liabilities						
Derivative instruments:						
Commodities	\$ (510)	\$ (130,166)	\$ (18,650)	\$ -	\$ 41,231	\$ (108,095)
Total derivative instruments	(510)	(130,166)	(18,650)	-	41,231	(108,095)
Total liabilities	<u>\$ (510)</u>	<u>(130,166)</u>	<u>\$ (18,650)</u>	<u>\$ -</u>	<u>\$ 41,231</u>	<u>\$ (108,095)</u>

The following table sets forth, by level within the fair value hierarchy, SRP's financial assets and liabilities that were accounted for at fair value on a recurring basis as of April 30, 2022 (in thousands):

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Other</u>	<u>Netting and Collateral</u>	<u>Total</u>
Assets						
Cash and cash equivalents:						
Money market funds	\$ -	\$ 474,000	\$ -	\$ -	\$ -	\$ 474,000
Total cash and cash equivalents	-	474,000	-	-	-	474,000
Non-utility property and other investments:						
Money market funds	-	21,953	-	-	-	21,953
Mutual funds	58,973	-	-	-	-	58,973
Total non-utility property and other investments	58,973	21,953	-	-	-	80,926
Segregated funds, net of current portion:						
Money market funds	-	4,837	-	-	-	4,837
Mutual funds	1,403,839	-	-	-	-	1,403,839
Commingled funds	-	-	-	274,683	-	274,683
Government securities	-	9,293	-	-	-	9,293
Total segregated funds, net of current portion	1,403,839	14,130	-	274,683	-	1,692,652
Current portion of segregated funds:						
Money market funds	-	99,177	-	-	-	99,177
Total current portion of segregated funds	-	99,177	-	-	-	99,177
Derivative instruments:						
Commodities	-	393,285	13,186	-	(279,317)	127,154
Total derivative instruments	-	393,285	13,186	-	(279,317)	127,154
Total assets	<u>\$1,462,812</u>	<u>\$1,002,545</u>	<u>\$ 13,186</u>	<u>\$ 274,683</u>	<u>\$ (279,317)</u>	<u>\$2,473,909</u>
Liabilities						
Derivative instruments:						
Commodities	\$ (2,531)	\$ (17,618)	\$ (20,546)	\$ -	\$ 18,354	\$ (22,341)
Total derivative instruments	(2,531)	(17,618)	(20,546)	-	18,354	(22,341)
Total liabilities	<u>\$ (2,531)</u>	<u>(17,618)</u>	<u>\$ (20,546)</u>	<u>\$ -</u>	<u>\$ 18,354</u>	<u>\$ (22,341)</u>

Valuation Methodologies

Securities

Money market funds: Investments with maturities of three months or less when purchased, including certain short-term fixed income securities, are considered cash equivalents. The fair value of shares in money market funds are priced based on inputs obtained from Bloomberg, a pricing service whose prices are obtained from direct feeds from exchanges, that are either directly or indirectly observable. Even though the NAV of the fund(s) is kept at \$1 per share, and transactions occur at that price, the underlying value of the securities may or may not be equal to \$1 per share; therefore, these funds are classified as Level 2 in the fair value hierarchy.

Mutual funds: The fair values of shares in mutual funds are based on inputs that are quoted prices in active markets for identical assets and, therefore, have been categorized as Level 1 in the fair value hierarchy. This category may include exchange-traded funds, which are similar to mutual funds in their structure but trade actively on exchanges like stocks. Mutual funds are priced using active market exchanges.

Commingled funds: Commingled funds are maintained by investment companies and hold certain investments in accordance with a stated set of fund objectives, which are consistent with SRP's overall investment strategy. For equity and fixed-income commingled funds, the fund administrator values the fund using the NAV per fund share, derived from the quoted prices in active markets of the underlying securities. Investments in non-publicly traded companies held in private equity funds are valued based on good-faith estimates of fair value performed by the fund manager. Commingled funds are measured at fair value using NAV as a practical expedient and are not

categorized in the fair value hierarchy. These assets are listed as “Other” in the fair value hierarchy to permit the reconciliation to amounts presented in the financial statements.

Government securities: The fair value of government securities is derived from quoted prices on similar assets in active or non-active markets, from pricing models whose inputs are observable for the substantially full term of the asset, or from pricing models whose inputs are derived principally from or corroborated by observable market data through correlation or other means; therefore, these securities have been categorized as Level 2 in the fair value hierarchy.

Commodity Derivative Instruments

The fair values of gas swaps and power swaps that are priced based on inputs using quoted prices of similar exchange-traded items have been categorized as Level 1 in the fair value hierarchy. These include gas and power swaps traded on exchanges.

The fair values of gas swaps, power swaps, gas options, power options and power deals that are priced based on inputs obtained through pricing agencies and developed pricing models, using similar observable items in active and inactive markets, are classified as Level 2 in the fair value hierarchy.

The fair values of derivative assets and liabilities that are valued using pricing models with significant unobservable market data traded in less active or underdeveloped markets are classified as Level 3 in the fair value hierarchy. Level 3 items include gas swaps, power swaps, gas options, power options and power deals. These inputs reflect management’s own assumptions about the assumptions a market participant would use in pricing the asset or liability.

SRP periodically transacts at locations, market price points or in time blocks that are non-standard or illiquid for which no prices are available from an independent pricing source. In these cases, SRP applies adjustments based on historical price curve relationships to a more liquid price point as a proxy for market prices. Such transactions are classified as Level 3.

SRP estimates the fair value of certain of its options using Black-Scholes option pricing models, which include inputs such as implied volatility, correlations, interest rates and forward price curves.

All the assumptions above include adjustments for counterparty credit risk, using credit default swap data, bond yields, when available, or external credit ratings.

SRP’s assessment of the significance of a particular input to the fair value measurements requires judgment and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels. SRP reviews the assumptions underlying its contracts monthly.

The following table provides quantitative information regarding significant unobservable inputs in SRP's Level 3 fair value measurements as of April 30, 2023:

	Fair Value (in thousands)		Unobservable Inputs	
	Assets	Liabilities	Range	Weighted Average*
Forward contracts	\$ -	\$ (1,125)		
Market price per MWh			\$88.40 - \$89.75	\$89.13
Market price per MMBtu			N/A	N/A
Option contracts	\$ -	\$ (17,525)		
Market price per MWh			\$39.42 - \$163.22	86.74
Power volatility			45.62%-138.37%	66.40%
Market price per MMBtu			\$2.81 - \$7.49	\$4.59
Gas volatility			44.80% - 86.30%	58.38%

*Unobservable inputs were weighted by the relative commodity quantity in each contract.

The following table provides quantitative information regarding significant unobservable inputs in SRP's Level 3 fair value measurements as of April 30, 2022:

	Fair Value (in thousands)		Unobservable Inputs	
	Assets	Liabilities	Range	Weighted Average*
Forward contracts	\$ 4,339	\$ (877)		
Market price per MWh			\$79.70 - \$86.15	\$82.92
Market price per MMBtu			\$3.07 - \$4.11	\$3.37
Option contracts	\$ 8,847	\$ (19,669)		
Market price per MWh			\$37.15 - \$182.26	\$82.77
Power volatility			20.5%-80.7%	35.3%
Market price per MMBtu			\$3.24 - \$9.09	\$3.49
Gas volatility			31.5% - 105.9%	34.1%

*Unobservable inputs were weighted by the relative commodity quantity in each contract.

See Note [7], DERIVATIVE INSTRUMENTS, for additional detail of derivatives.

Investments Calculated at Net Asset Value

As of April 30, 2023, the fair value measurement of investments calculated at NAV (or its equivalent), as well as the nature and risks of those investments, is as follows:

	Fair Value (in thousands)	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Commingled funds:				
Fixed income funds	\$ 285,241	None	Daily	N/A
Private equity fund	811	\$4.0 million	N/A	N/A
Total commingled funds	<u>\$ 286,052</u>			

As of April 30, 2022, the fair value measurement of investments calculated at NAV (or its equivalent), as well as the nature and risks of those investments, is as follows:

	<u>Fair Value</u> <i>(in thousands)</i>	<u>Unfunded</u> <u>Commitments</u>	<u>Redemption</u> <u>Frequency</u>	<u>Redemption</u> <u>Notice Period</u>
Commingled funds:				
Fixed income funds	\$ 274,083	None	Daily	N/A
Private equity fund	600	\$4.4 million	N/A	N/A
Total commingled funds	<u>\$ 274,683</u>			

Fixed income commingled funds: These funds are actively managed funds used by an investment manager to diversify an overall portfolio of separately managed fixed-income securities. The funds may invest in fixed-income securities of varying duration, maturity, credit quality and geographic location. The securities may be non-U.S. securities.

Private equity commingled fund: This fund invests primarily in privately held early stage and emerging growth technology companies and businesses primarily based in, or having existing or potential strategic and economic ties to, the State of Arizona.

Margin and Collateral Deposits

Margin and collateral deposit assets and liabilities include cash deposited with, and received from, counterparties and brokers as credit support under energy contracts. The amount of margin and collateral deposits varies based on changes in the fair value of the positions. SRP presents its margin and cash collateral deposits net with its derivative positions on the accompanying Combined Balance Sheets. Net margin and collateral deposits (liabilities) were (\$13.4 million) and (\$261.0 million) as of April 30, 2023 and 2022, respectively. The significant increase in collateral held by SRP is due to market value changes of SRP's natural gas and fuel contracts. See Note [7], DERIVATIVE INSTRUMENTS.

Changes in Level 3 Fair Value Measurements

The tables below include the reconciliation of changes to the balance sheet amounts for the fiscal years ended April 30 for commodity derivative instruments classified as Level 3 in the fair value hierarchy; this determination is based upon unobservable inputs to the overall fair value measurement (in thousands):

	<u>2023</u>	<u>2022</u>
Beginning balance, May 1	\$ (7,360)	\$ (61,592)
Transfers out of Level 3	(12,586)	25,792
Net realized and unrealized gain (loss) included in earnings	(5,255)	22,860
Net purchases (sales)	(103)	(780)
Settlements	6,654	6,360
Ending balance, April 30	<u>\$ (18,650)</u>	<u>\$ (7,360)</u>

Realized and unrealized gains and losses included in earnings identified above are included in wholesale revenues, power purchased or fuel used in electric generation, as appropriate in the accompanying Combined Statements of Net Revenues. The transfers out of Level 3 for each fiscal year primarily represent derivative positions for which the maturity date has moved to within a time frame such that there are published price curves available to use for performing the valuations.

Fair Value Disclosures

U.S. GAAP requires disclosure of the estimated fair value of certain financial instruments and the methods and significant assumptions used to estimate their fair values. Many but not all of the financial instruments are recorded at fair value on the accompanying Combined Balance Sheets. Financial instruments held by SRP are discussed below.

Financial instruments for which fair value approximates carrying value: Certain financial instruments that are not carried at fair value on the accompanying Combined Balance Sheets are carried at amounts that approximate fair value due to their short-term nature and generally negligible credit risk. The instruments include receivables, accounts payable, customers' deposits, other current liabilities, commercial paper and loans against the District's revolving line-of-credit agreements.

Financial instruments for which fair value does not approximate carrying value: SRP presents long-term debt at carrying value on the accompanying Combined Balance Sheets. The collective fair value of the District's revenue bonds, including the current portion, was estimated by using industry leading pricing services from independent sources. As of April 30, 2023 and 2022, the carrying amount of the District's revenue bonds, including current portion and accrued interest, was \$4.8 billion and \$4.4 billion, respectively, and the estimated fair value was \$4.6 billion and \$4.3 billion, respectively. These estimated fair values are classified as Level 2 in the fair value hierarchy. (See Note [9], LONG-TERM DEBT, for further discussion of the District's revenue bonds.)

(9) LONG-TERM DEBT:

Long-term debt consists of the following as of April 30 (in thousands):

	<u>Maturity</u>	<u>Interest Rate</u>	<u>2023</u>	<u>2022</u>
Revenue bonds				
2010 Series A	2040 – 2041	4.84%	\$ 490,915	\$ 490,915
2015 Series A	2026 – 2045	3.00%-5.00%	867,285	873,780
2016 Series A	2024 – 2038	4.00%-5.00%	652,960	681,160
2017 Series A	2024 – 2039	5.00%	657,415	684,910
2019 Series A	2024 – 2049	3.00%-5.00%	438,745	446,240
2020 Series A	2025 – 2048	2.38%-5.00%	177,330	190,550
2020 Series B	2048 – 2050	2.57%	100,000	100,000
2021 Series A	2024 – 2029	5.00%	251,395	277,400
2022 Series A	2030 – 2032	5.00%	193,065	193,065
2023 Series A	2029 – 2050	5.00%	500,000	-
Total revenue bonds			4,329,110	3,938,020
Unamortized bond premium (discount), net			419,979	411,314
Unamortized debt issuance costs			(9,259)	(8,437)
Total revenue bonds outstanding			4,739,830	4,340,897
Revolving line-of-credit loan			-	3,500
Commercial paper			325,000	325,000
Total long-term debt and short-term debt			5,064,830	4,669,397
Less: Current portion of long-term debt			(113,930)	(108,910)
Total long-term debt			<u>\$ 4,950,900</u>	<u>\$ 4,560,487</u>

The annual maturities of revenue bonds as of April 30, 2023, due in fiscal years ending April 30, are as follows (in thousands):

2024	\$	113,930
2025		118,780
2026		126,415
2027		129,205
2028		142,690
Thereafter		<u>3,698,090</u>
Total	\$	<u><u>4,329,110</u></u>

Revenue Bonds

Revenue bonds are secured by a pledge of, and a lien on, the revenues of the electric system, after deducting operating expenses, as defined in the amended and restated bond resolution, effective in January 2003, as amended (Bond Resolution). The Bond Resolution requires the District to charge and collect revenues sufficient to fund the debt reserve account and pay operating expenses, debt service and all other charges and liens payable out of revenues and income. Under the terms of the Bond Resolution, the District makes debt service deposits to a non-trusted segregated fund. Included in segregated funds in the accompanying Combined Balance Sheets are \$185.3 million and \$179.8 million of debt-service related funds as of April 30, 2023 and 2022, respectively. Additionally, the Bond Resolution requires the District to maintain a debt service coverage ratio of 1.1 or greater on outstanding revenue bonds. To be eligible to issue additional revenue bonds, the District must anticipate sufficient revenues to maintain that ratio post-issuance. For the fiscal years ended April 30, 2023 and 2022, the debt service coverage ratio was 3.6 and 3.5, respectively. A substantial portion of the revenue bonds are callable by the District ten years after issuance.

In October 2010, the District issued \$500.0 million of 2010 Series A Electric System Revenue Bonds as federally taxable, direct payment “Build America Bonds” under the American Recovery and Reinvestment Act of 2009 (ARRA). At the time of issuance, the District expected, in accordance with the ARRA, to receive subsidy payments from the United States Treasury equal to 35% of the interest paid on the 2010 Series A Bonds over the entire term of the bonds.

Due to federal budget sequestration, beginning March 2013, the Internal Revenue Service has reduced the subsidy amounts paid to issuers of Build America Bonds each year. The District’s semi-annual subsidy payments have been reduced by amounts ranging from 5.7% to 8.7%. Subject to the District’s compliance with certain provisions of the ARRA and including the effect of reductions for sequestration, the District recorded \$7.8 million for subsidy earned during the fiscal years ending April 30, 2023 and 2022. The subsidy earned is included in the accompanying Combined Statements of Net Revenues as a reduction to interest on bonds, net. The balance of subsidy payments receivable was \$2.6 million as of April 30, 2023 and 2022.

In September 2021, the District issued \$277.4 million of Series A Electric System Revenue Bonds at an average effective interest rate of 1.0%. The proceeds of the bonds, along with a \$4.0 million contribution from the District, were deposited into an externally trusted irrevocable account. The escrow account was used to refund all outstanding 2011 Series A Bonds, which have been removed from SRP’s Combined Balance Sheet. The refunding is a non-cash activity on the Combined Statements of Cash Flows, except for the \$4.0 million contribution which is a cash outflow for financing activities.

In March 2022, the District issued \$193.1 million of Series A Electric System Revenue Bonds at an average effective interest rate of 2.1%. The proceeds of the bonds, along with a \$3.0 million contribution from the District, were deposited into an externally trusted irrevocable account. The escrow account was used to refund all outstanding 2012 Series A Bonds, which have been removed from SRP’s Combined Balance Sheet. The refunding is a non-cash

activity on the Combined Statements of Cash Flows, except for the \$3.0 million contribution which is a cash outflow for financing activities.

In April 2022, the District entered into a forward delivery contract to issue \$277.9 million of Series A Electric System Revenue Bonds in March 2025. The proceeds of the bonds will be used to refund \$300.0 million of 2015 Series A Bonds outstanding in March 2025. The transaction will be reflected in the Combined Financial Statements for the fiscal year ending April 30, 2025.

In February 2023, the District issued \$500.0 million of 2023 Series A Electric System Revenue Bonds at an average effective interest rate of 4.2%. The proceeds of the bonds were used to pay costs of issuance and will fund capital improvements of the District.

Interest, Build America Bonds subsidy payments, and the amortization of bond discount, premium and issuance costs on the various issues result in an effective rate of 3.5% over the remaining term of the bonds.

As of April 30, 2023, the District had authorization to issue additional Electric System Revenue Bonds totaling \$1.8 billion in principal amount and Electric System Refunding Revenue Bonds totaling \$5.1 billion principal amount.

(10) COMMERCIAL PAPER AND CREDIT AGREEMENTS:

The District is authorized by the Board to issue up to \$800.0 million in commercial paper. The District had \$50.0 million of Series C Commercial Paper outstanding as of April 30, 2023 and 2022, and an additional \$275.0 million of Series D-1 Commercial Paper outstanding as of April 30, 2023 and 2022. As of April 30, 2023 and 2022, the Series C issue had a weighted average interest rate to the District of 3.15% and 0.54%, respectively. As of April 30, 2023 and 2022, the Series D-1 issue had a weighted average interest rate to the District of 4.94% and 0.58%, respectively. The commercial paper matures not more than 270 days from the date of issuance and is an unsecured obligation of the District.

As of April 30, 2023, the District has four revolving line-of-credit agreements (in thousands):

Credit Institution	Credit Amount	Expiration
U.S. Bank National Association	\$ 200,000	June 28, 2024
Bank of America, N.A.	250,000	December 9, 2025
J.P. Morgan Chase Bank, National Association	175,000	June 29, 2026
TD Bank, N.A.	175,000	July 14, 2026

The revolving line-of-credit agreements support the \$325.0 million of outstanding commercial paper as of April 30, 2023. Commercial paper is classified as long-term debt in the accompanying Combined Balance Sheets.

The revolving line-of-credit agreements contain various conditions precedent to borrowings that include, but are not limited to, compliance with the covenants set forth in the agreements, the continued accuracy of representations and warranties, no existence of default, and maintenance of certain investment grade ratings on the District’s revenue bonds. The District was in compliance with the various covenants as of April 30, 2023 and 2022. Alternative sources of funds to support the commercial paper program include existing funds on hand or the issuance of alternative debt, such as revenue bonds.

The remaining unallocated \$475.0 million in credit available under the four lines of credit as of April 30, 2023, may be used to support the issuance of additional commercial paper or for other general corporate purposes.

(11) LEASES:

SRP leases land, buildings, equipment and other property to facilitate operations of generating stations through operating rental agreements with varying terms, provisions and expiration dates. SRP also has certain power purchase agreements that qualify as lease arrangements (PPA Leases). SRP's leases have remaining terms that expire in 2024 through 2045.

Lessee

SRP enters into various agreements to purchase power, electric capacity and other energy products that may be accounted for as a lease when SRP has the right to determine when and how the generating unit operates or is designed. SRP may elect to terminate certain leases if the projects are decommissioned or otherwise permanently removed from service. SRP's lease agreements do not contain any material residual value guarantees or restrictive covenants.

SRP recognizes lease assets and liabilities upon lease commencement. The following table provides information related to the classification of lease balances on the Combined Balance Sheets as of April 30 (in thousands):

	<u>2023</u>	<u>2022</u>
Assets		
Other deferred charges and other assets		
Operating lease right-of-use assets	\$ 89,153	\$ 96,163
Total lease assets	<u>\$ 89,153</u>	<u>\$ 96,163</u>
Liabilities		
Other current liabilities		
Short-term operating lease liabilities	\$ 7,031	\$ 7,058
Other deferred credits and other non-current liabilities		
Long-term operating lease liabilities	56,602	61,247
Total lease liabilities	<u>\$ 63,633</u>	<u>\$ 68,305</u>

The following table provides information related to SRP's lease costs for the fiscal year ended April 30, 2023 (in thousands):

	<u>PPA Leases</u>	<u>Other Leases</u>	<u>Total</u>
Operating lease cost	\$ -	\$ 9,393	\$ 9,393
Variable lease cost	143,234	-	143,234
Short-term lease cost	-	597	597
Total	<u>\$ 143,234</u>	<u>\$ 9,990</u>	<u>\$ 153,224</u>

The following table provides information related to SRP's lease costs for the fiscal year ended April 30, 2022 (in thousands):

	<u>PPA Leases</u>	<u>Other Leases</u>	<u>Total</u>
Operating lease cost	\$ -	\$ 9,382	\$ 9,382
Variable lease cost	137,206	1,951	139,157
Short-term lease cost	-	783	783
Total	<u>\$ 137,206</u>	<u>\$ 12,116</u>	<u>\$ 149,322</u>

Lease costs related to PPA Leases are recorded in power purchased in the Combined Statements of Net Revenues. Lease costs for other leases are included as a component of operating expenses in the accompanying Combined

Statements of Net Revenues. Variable lease costs are recognized in the period the costs are incurred and primarily relate to renewable energy PPA Leases. Payments under most renewable energy PPA Leases are dependent upon environmental factors, and due to the inherent uncertainty associated with the reliability of the energy source, the payments are considered variable and are excluded from the measurement of lease liabilities and right-of-use lease assets.

The following maturity analysis reconciles expected undiscounted cash flows in years ending April 30 to the operating lease liability as of April 30, 2023 (in thousands):

2024	\$	7,058
2025		7,064
2026		7,069
2027		7,075
2028		7,081
Thereafter		34,772
Total lease commitments		<u>70,119</u>
Less: interest		<u>(6,486)</u>
Total	\$	<u>63,633</u>

The following table provides additional information related to operating lease liabilities, as of April 30:

	<u>2023</u>	<u>2022</u>
Weighted-average remaining lease term	12 years	13 years
Weighted-average discount rate*	1.83%	1.83%
Cash paid for leasing arrangements (operating cash flow), in millions	\$7.1	\$7.1

*When an implicit rate is not readily determinable, an incremental borrowing rate is utilized, determining the present value of lease payments. The rate is based on expected term and information available at the commencement date.

Lessor

SRP leases land and other assets to third parties that are classified as operating leases. These leases have varying terms, provisions, expiration dates and term extension options. Remaining lease terms range from 1 to 92 years. Lease income is reported in other income in the accompanying Combined Statements of Net Revenues. During the fiscal years ended April 30, 2023 and 2022, lease income was \$8.5 million and \$7.4 million, respectively.

The undiscounted cash flows to be received from lease payments in fiscal years ending April 30 are summarized below (in thousands):

2024	\$	7,909
2025		7,875
2026		7,906
2027		7,942
2028		7,924
Thereafter		863,578
Total	\$	<u>903,134</u>

(12) EMPLOYEE BENEFIT PLANS AND INCENTIVE PROGRAMS:

Defined Benefit Pension Plan and Other Post-retirement Benefits

SRP’s Employees’ Retirement Plan (the Plan) covers substantially all employees. The Plan is funded entirely from SRP contributions and the income earned on invested Plan assets. SRP contributed \$75.0 million in each fiscal year ended April 30, 2023 and 2022.

SRP provides a non-contributory defined benefit medical plan for retired employees and their eligible dependents (contributory for employees hired January 1, 2000, or later) and a non-contributory defined benefit life insurance plan for retired employees. Employees are eligible for coverage if they retire at age 65 or older with at least five years of vested service under the Plan (ten years for those hired January 1, 2000, or later), or at any time after attainment of age 55 with a minimum of ten years of vested service under the Plan (twenty years for those hired January 1, 2000, or later). The funding policy is discretionary.

During fiscal year 2023, the Board approved an ad-hoc Cost-of-Living-Adjustment (COLA) for select participants receiving benefits from the Plan, effective May 1, 2023. Participants who retired prior to 2013 were provided a graded increase to their benefits ranging from 2.7% for a 2012 retiree, to 27% for a 1982 or earlier retiree. The COLA increased the Projected Benefit Obligation (PBO) by approximately \$35.0 million and the projected fiscal year 2024 expense by approximately \$4.5 million.

U.S. GAAP requires employers to recognize the overfunded or underfunded positions of defined benefit pension and other post-retirement plans in their balance sheets. Any actuarial gains and losses, prior service costs and transition assets or obligations must be recorded on the balance sheet with an offset to accumulated other comprehensive income until the amounts are amortized as a component of net periodic benefit costs.

The Board has authorized the District to collect future amounts associated with the pension and other post-retirement plan liabilities as part of the pricing process. The District established a regulatory asset for the amounts otherwise chargeable to accumulated other comprehensive income that are expected to be recovered through prices in future periods. The changes in actuarial gains and losses, prior service costs and transition assets or obligations pertaining to the regulatory asset are recognized as an adjustment to the regulatory asset or liability accounts, as these amounts are recognized as components of net periodic pension costs each fiscal year. The District’s amortization amounts for fiscal year 2023 were \$2.1 million for prior service cost and \$16.0 million for net actuarial loss. The District’s amortization amounts for fiscal year 2022 were \$1.3 million for prior service cost and \$61.4 million for net actuarial loss.

The following tables outline changes in benefit obligations, plan assets, the funded status of the plans and amounts included in the accompanying Combined Financial Statements, as of and for the years ended April 30 (in thousands):

	Pension Benefits		Post-retirement Benefits	
	2023	2022	2023	2022
Change in benefit obligation				
Benefit obligation at beginning of year	\$ 2,781,007	\$ 3,214,615	\$ 755,302	\$ 950,365
Service cost	77,316	101,747	19,603	26,886
Interest cost	122,242	106,893	33,214	31,618
Actuarial gain	(240,364)	(518,304)	(48,750)	(218,009)
Benefits paid	(129,562)	(123,944)	(34,337)	(35,558)
Plan amendment (COLA)	34,996	-	-	-
Benefit obligation at end of year	<u>2,645,635</u>	<u>2,781,007</u>	<u>725,032</u>	<u>755,302</u>
Change in plan assets				
Fair value of plan assets at beginning of year	2,653,952	2,859,963	-	-
Actual return on plan assets	24,259	(157,067)	-	-
Employer contributions	75,000	75,000	34,337	35,558
Benefits paid	(129,562)	(123,944)	(34,337)	(35,558)
Fair value of plan assets at end of year	<u>2,623,649</u>	<u>2,653,952</u>	<u>-</u>	<u>-</u>
Funded status at end of year	<u>\$ (21,986)</u>	<u>\$ (127,055)</u>	<u>\$ (725,032)</u>	<u>\$ (755,302)</u>
Amounts recognized in Combined Balance Sheets				
Other current liabilities	\$ -	\$ -	\$ (33,382)	\$ (33,673)
Accrued post-retirement liability	(21,986)	(127,055)	(691,650)	(721,629)
Net liability recognized	<u>\$ (21,986)</u>	<u>\$ (127,055)</u>	<u>\$ (725,032)</u>	<u>\$ (755,302)</u>
Amounts recognized as a regulatory asset				
Prior service cost (credit)	\$ 53,086	\$ 20,158	\$ 312	\$ 380
Net actuarial loss (gain)	494,175	566,264	(54,541)	(5,272)
Net regulatory asset	<u>\$ 547,261</u>	<u>\$ 586,422</u>	<u>\$ (54,229)</u>	<u>\$ (4,892)</u>

Actuarial gains related to changes in the benefit obligation during the year ended April 30, 2023 were \$240.4 million and \$48.8 million for pension benefits and post-retirement benefits, respectively, primarily due to a change in the discount rate from 4.50% in fiscal year 2022 to 5.13% in fiscal year 2023.

Actuarial gains related to changes in the benefit obligation during the year ended April 30, 2022 were \$518.3 million and \$218.0 million for pension benefits and post-retirement benefits, respectively, primarily due to a change in the discount rate from 3.39% in fiscal year 2021 to 4.50% in fiscal year 2022.

The accumulated benefit obligation for pension benefits was \$2.4 billion and \$2.5 billion as of April 30, 2023 and 2022, respectively.

SRP internally funds its other post-retirement benefits obligation. As of April 30, 2023 and 2022, \$1.1 billion of segregated funds were designated for this purpose.

The weighted-average assumptions used to calculate actuarial present values of benefit obligations as of April 30 were as follows:

	Pension Benefits		Post-retirement Benefits	
	2023	2022	2023	2022
Discount rate	5.13%	4.50%	5.13%	4.50%
Rate of compensation increase	4.70%	4.70%	N/A	N/A

Weighted-average assumptions used to calculate net periodic benefit costs were as follows:

	Pension Benefits		Post-retirement Benefits	
	2023	2022	2023	2022
Discount rate	4.50%	3.39%	4.50%	3.39%
Expected return on Plan assets	7.75%	7.75%	N/A	N/A
Rate of compensation increase	4.70%	4.70%	N/A	N/A

A 6.50% annual increase in per capita costs of healthcare benefits was assumed during fiscal year 2023; these rates were assumed to decrease uniformly until equaling 4.75% in all future years.

The components of net periodic benefit costs for the fiscal years ended April 30 are as follows (in thousands):

	Pension Benefits		Post-retirement Benefits	
	2023	2022	2023	2022
Service cost	\$ 77,316	\$ 101,747	\$ 19,603	\$ 26,886
Interest cost	122,242	106,893	33,214	31,618
Expected return on Plan assets	(207,980)	(197,630)	-	-
Amortization of net actuarial loss	15,446	53,275	519	8,080
Amortization of prior service cost	2,068	2,068	68	(787)
Net periodic benefit cost	<u>\$ 9,092</u>	<u>\$ 66,353</u>	<u>\$ 53,404</u>	<u>\$ 65,797</u>

Plan Assets

The Board has established an investment policy for Plan assets and has delegated oversight of such assets to a compensation committee (the Committee). The investment policy sets forth the objective of providing for future pension benefits by targeting returns consistent with a stated tolerance of risk. The investment policy is based on analysis of the characteristics of the Plan sponsors, actuarial factors, current Plan condition, liquidity needs and legal requirements. The primary investment strategies are diversification of assets, stated asset allocation targets and ranges, and external management of Plan assets. The Committee determines the overall target asset allocation ratio for the Plan and defines the target asset allocation ratio deemed most appropriate for the needs of the Plan and the risk tolerance of the District.

The market value of investments (reflecting returns, contributions and benefit payments) within the Plan trust appreciated 0.93% during fiscal year 2023, compared to depreciation of 5.59% during fiscal year 2022. Changes in the Plan's funded status affect the assets and liabilities recorded on the Combined Balance Sheets in accordance with authoritative guidance for regulated enterprises. Due to the District's regulatory treatment, the recognition of funded status is offset by regulatory assets or liabilities and is recovered through customer rates. There have been numerous legislative changes in recent years that have affected funding requirements. The Moving Ahead for Progress in the 21st Century Act (MAP-21), the Highway and Transportation Funding Act of 2014 (HAFTA), the Bipartisan Budget Act of 2015 (BBA15), the American Rescue Plan Act of 2021 (ARPA), and the Infrastructure Investment and Jobs Act (IIJA) were signed into law at the end of 2021. All of these acts have decreased the level of minimum required contributions.

The Plan's weighted-average asset allocations as of April 30 are as follows:

	Target Allocations	2023	2022
Equity securities	65%	63%	65%
Debt securities	25%	26%	23%
Real estate	10%	11%	12%
Total	100%	100%	100%

The investment policy, as authorized by the Board, allows management to reallocate Plan assets at any time within a tolerance range up to plus or minus 5% from the target asset allocation which allows for flexibility in managing the assets based on prevailing market conditions and does not require automatic rebalancing if the actual allocation strays from the target allocation.

Fair Value of Plan Assets

Assets measured at fair value using NAV are not categorized in the fair value hierarchy. These assets are listed in the column "Other" in the following tables to permit reconciliation to amounts presented elsewhere.

The following table sets forth the fair value of Plan assets, by asset category, as of April 30, 2023 (in thousands):

	Level 1	Level 2	Other	Total
Cash and cash equivalents	\$ 29,680	\$ -	\$ -	\$ 29,680
Mutual funds	120,179	-	-	120,179
Government securities	-	103,421	-	103,421
Corporate bonds	-	572,458	-	572,458
Common stocks	81,449	-	-	81,449
Commingled funds	-	-	1,427,533	1,427,533
Real estate	-	-	288,929	288,929
Total assets	<u>\$ 231,308</u>	<u>\$ 675,879</u>	<u>\$ 1,716,462</u>	<u>\$ 2,623,649</u>

The following table sets forth the fair value of Plan assets, by asset category, as of April 30, 2022 (in thousands):

	Level 1	Level 2	Other	Total
Cash and cash equivalents	\$ 46,670	\$ -	\$ -	\$ 46,670
Mutual funds	154,373	-	-	154,373
Government securities	-	79,587	-	79,587
Corporate bonds	-	526,175	-	526,175
Common stocks	91,776	-	-	91,776
Commingled funds	-	-	1,439,601	1,439,601
Real estate	-	-	315,770	315,770
Total assets	<u>\$ 292,819</u>	<u>\$ 605,762</u>	<u>\$ 1,755,371</u>	<u>\$ 2,653,952</u>

For a description of the fair value hierarchy, refer to Note [8], FAIR VALUE MEASUREMENTS.

Valuation Methodologies

Corporate bonds: For fixed-income securities, multiple prices and price types are obtained from pricing vendors whenever possible, which enables cross-provider validations in addition to checks for unusual daily movements. A primary price source is identified based on asset type, class or issue for each security. SRP has obtained an understanding of how these prices are derived, including the nature and observability of the inputs used in

deriving such prices. Additionally, SRP selectively corroborates the fair values of securities by comparison to other market-based price sources. The fair values of fixed-income securities are based on evaluated prices that reflect observable market information, such as actual trade information of similar securities, adjusted for observable differences, and are categorized as Level 2.

Common stocks: The fair values of shares in preferred and common corporate stocks are based on inputs that are quoted prices in active markets for identical assets and, therefore, have been categorized as Level 1 in the fair value hierarchy. Equity securities held individually are primarily traded on exchanges that contain only actively traded securities due to the volume trading requirements imposed by these exchanges. Common stocks that are valued based on quoted prices from less active markets, such as over-the-counter stocks, are categorized as Level 2 in the fair value hierarchy.

Real estate: Real estate commingled funds are funds with a direct investment in a pool of real estate properties. These funds are valued by investment managers on a periodic basis using pricing models that use independent appraisals from sources with professional qualifications. The valuations of the real estate funds are sensitive to market factors outside the control of the Plan, including interest rate levels and economic activity. The valuations, although done quarterly by independent qualified appraisers, may vary due to these factors.

For an explanation of the valuation methodologies used to determine fair value of the assets of the Plan that are not listed above, refer to Note [8], FAIR VALUE MEASUREMENTS.

Long-term Rate of Return

The expected return on Plan assets is based on a review of the Plan asset allocations and consultations with a third-party investment consultant and the Plan actuary, considering market and economic indicators, historical market returns, correlations and volatility, and recent professional or academic research.

Employer Contributions

SRP expects to contribute \$75.0 million to the Plan over the next fiscal year.

Benefits Payments

SRP expects to pay benefits in the amounts as follows in fiscal years ending April 30 (in thousands):

	Post-retirement Benefits		
	Pension Benefits	Before Subsidy*	Net
2024	\$ 138,161	\$ 34,228	\$ 33,473
2025	142,349	35,361	34,598
2026	146,109	36,445	35,683
2027	149,811	37,608	36,848
2028	153,369	38,688	37,934
2029 through 2033	815,781	209,632	206,083

*Estimated future benefit payments, including prescription drug benefits, prior to federal drug subsidy receipts expected as a result of the Medicare Prescription Drug, Improvement and Modernization Act of 2003.

Defined Contribution Plan

SRP’s Employees’ 401(k) Plan (the 401(k) Plan) covers substantially all employees. The 401(k) Plan receives employee pre-tax and post-tax contributions and partial employer matching contributions. Employees who have one year of service in which they have worked at least 1,000 hours and who are also contributing to the 401(k) Plan are eligible to receive partial employer matching contributions of \$0.90 on every dollar contributed up to the

first 6% of their base pay that they contribute to the 401(k) Plan. Employer matching contributions to the 401(k) Plan were \$25.4 million and \$24.5 million during fiscal years ended April 30, 2023 and 2022, respectively.

Employee Performance Incentive Compensation Program

The EPIC program, a cash-based incentive program, covers substantially all regular employees and is based on the achievement of pre-established targets for each fiscal year. The total compensation expense, including payroll taxes, recognized for the EPIC program for fiscal years ended April 30, 2023 and 2022 was \$33.0 million and \$37.4 million, respectively.

Employee Sick Leave Plan

The SRP Employee Sick Leave Plan provides payment to employees for unused sick leave. Employees accumulate sick days at a rate of one day per month. The accumulation, up to the personal maximum, can be carried forward year after year. For most employees, the personal maximum is 720 hours. For sick leave hours accumulated in excess of the personal maximum, a lump sum payment at half pay is made annually in January of each year based on the hourly rate at time of payment, and the accumulated sick leave is then returned to the personal maximum. Upon death or retirement, payment is made for any unused sick leave hours. The payments for death or retirement are based on the hourly rate of pay at death or retirement. SRP has an accrual for unpaid sick leave of approximately \$59.8 million and \$61.6 million as of April 30, 2023 and 2022, respectively. The accrual is recorded in other current liabilities and other deferred credits and noncurrent liabilities on the Combined Balance Sheets. The accrual is determined actuarially based on various assumptions, including future pay raises, discount rate and the amount of the accrual that will ultimately be paid out.

(13) INTERESTS IN JOINTLY OWNED ELECTRIC UTILITY PLANTS AND TRANSMISSION FACILITIES:

The District has entered into various agreements with other electric utilities for the joint ownership of electric generating and transmission facilities. Each participating owner in these facilities must provide for the cost of its ownership share. The District's share of expenses of the jointly owned plants and transmission facilities is included in operations and maintenance expense in the accompanying Combined Statements of Net Revenues.

The following table reflects the District's ownership interests in jointly owned facilities at electric utility plants as of April 30, 2023 (in thousands):

Generating Station	Ownership Share	Plant in Service	Accumulated Depreciation	Construction Work in Progress
Four Corners (NM) (Units 4 & 5)	10.00%	\$ 286,500	\$ (203,114)	\$ 4,947
Hayden (CO) (Unit 2)	50.00%	190,185	(167,651)	1,178
Craig (CO) (Units 1 & 2)	29.00%	368,564	(333,391)	1,157
Mesquite Common (AZ)	50.00%	85,840	(14,663)	74
PVNGS (AZ) (Units 1, 2 & 3)	20.13%	1,642,410	(1,158,555)	33,777
Springerville Common (AZ)	17.05%-50.00%	45,444	(9,557)	937
Gila River Common (AZ)	50.00%	67,291	(5,447)	843
Total		\$ 2,686,234	\$ (1,892,378)	\$ 42,913

In February 2017, the non-federal owners of NGS decided to discontinue their participation in the plant beyond the end of the then existing lease with the Navajo Nation for the land on which the plant was constructed. In December 2019, the lease ended and decommissioning activities, including required monitoring activities, began and will continue for thirty-four years. The District holds a 23.2% decommissioning participation rate;

consequently, the District owns 23.2% of the monitoring assets and their infrastructure which will remain at NGS and will be depreciated over their remaining life.

The following table reflects the District's investment in jointly owned transmission facilities as of April 30, 2023 (in thousands):

Transmission Facility	Plant in Service	Accumulated Depreciation	Construction Work in Progress
Mead Phoenix	\$ 54,033	\$ (23,840)	\$ 82
Southwest Valley	97,457	(26,761)	5,592
Southeast Valley	303,195	(65,511)	1,198
Morgan-Pinnacle Peak	73,008	(16,984)	-
Southern Transmission	62,023	(41,007)	795
Mesquite	17,269	(6,499)	393
ANPP	94,285	(35,624)	4,087
Kyrene-Knox	12,443	(2,043)	2
Total	\$ 713,713	\$ (218,269)	\$ 12,149

The District's ownership interests in the jointly owned transmission facilities vary by facility and for the various projects within each facility.

(14) VARIABLE INTEREST ENTITIES:

SRP follows guidance that defines a variable interest entity (VIE) as a legal entity whose equity owners do not have sufficient equity at risk or lack certain characteristics of a controlling financial interest in the entity. This guidance identifies the primary beneficiary as the variable interest holder that has the power to direct the activities that most significantly affect the VIE's economic performance (power criterion) and has the obligation to absorb losses or the right to receive benefits from the VIE (losses/benefits criterion). The primary beneficiary is required to consolidate the VIE unless specific exceptions or exclusions are met. SRP considers both qualitative and quantitative factors to form a conclusion whether it, or another interest holder, meets the power criterion and the losses/benefits criterion. SRP performs ongoing reassessments of its VIEs to determine if the primary beneficiary changes each reporting period.

Unconsolidated VIEs

While SRP is not required to consolidate any VIE as of April 30, 2023 or 2022, it held variable interests in certain VIEs as described below.

The District has entered into various long-term power purchase agreements with renewable energy generation facilities that extend for periods of 20 to 30 years. The District receives the power and renewable energy credits from these facilities. The capacity of all these facilities combined is approximately 298 MW. The amounts that the District paid to these projects were \$125.1 million and \$119.0 million for fiscal years 2023 and 2022, respectively. With the exception of projects for which the District is obligated to pay operating and maintenance expenses, the District is obligated to pay only for actual energy delivered and will have no obligation with respect to any facilities that do not start commercial operations. Some of these agreements include a price adjustment clause that will affect the future cost. While certain of these agreements provide a minimum production or performance guarantee, the District considers all production-based payments from renewable fuel source facilities to be contingent on future production of the facility. Therefore, even though certain of these agreements may be considered finance leases, SRP has not recorded a finance lease obligation for guaranteed minimum lease

payments due to the contingent nature of such payments. The District has concluded that it is not the primary beneficiary of these VIEs since it does not control operations and maintenance, which it believes are the primary activities that most significantly affect the economic activities of the entity.

The District is a part owner of a limited liability company (LLC) formed during fiscal year 2010 to market long-term water storage credits. The District did not make capital contributions nor receive capital distributions in fiscal year 2023. In fiscal year 2022, the District received net capital distributions of \$3.3 million. The District’s investment in the LLC was \$6.1 million and \$5.8 million as of April 30, 2023 and 2022, respectively. The District accounts for its investment in the LLC as an equity method investment within non-utility property and other investments in the accompanying Combined Balance Sheets. The District has a future maximum exposure up to a \$25.0 million contribution limit. The primary risks associated with this VIE relate to the marketing of the water storage credits. The District has concluded that it is not the primary beneficiary of this VIE since it does not have power to direct the activities related to the marketing of the long-term water storage credits, which it believes are the primary activities that most significantly affect the economic activities of the entity.

(15) COMMITMENTS AND CONTINGENCIES:

Purchased Power and Fuel Supply

The District had various firm, non-cancelable purchase commitments as of April 30, 2023, which are not recognized in the accompanying Combined Balance Sheets. The following table presents estimated future payments pertaining to firm purchase commitments with remaining terms greater than one year (in thousands):

	Purchased Power Contracts	Fuel Supply Contracts	Total
2024	\$ 27,771	\$ 287,945	\$ 315,716
2025	27,994	236,678	264,672
2026	28,223	169,220	197,443
2027	28,442	93,552	121,994
2028	28,735	86,974	115,709
Thereafter	244,643	206,811	451,454

In addition to the commitments in the table above, the District has long-term commodity purchase agreements described below.

Gas Purchase Agreement

In October 2007, the District entered into a 30-year gas purchase agreement with Salt Verde Financial Corporation (SVFC), an Arizona nonprofit corporation formed for the primary purpose of supplying natural gas to the District. Under the agreement, the District is committed to purchase 10,420,000 MMBtu each year during fiscal years 2024 through 2028, and 104,200,000 MMBtu over the balance of the term. The District receives a discount from market prices and is obligated to pay only for gas delivered. Payments, net of the discount, to SVFC under the agreement were \$70.1 million and \$29.5 million in fiscal years 2023 and 2022, respectively. The agreement also provides for payment from SVFC to the District of certain excess cash resulting from a portion of SVFC’s investment income, which effectively reduces the price the District pays for the gas. The excess cash amounts received by the District from SVFC were \$3.0 million and \$3.1 million in fiscal years 2023 and 2022, respectively. SVFC is a related party to the District.

Commodity Purchase Agreement

In April 2021, the District entered into a commodity purchase agreement with Southeast Energy Authority (SEA), a Cooperative District and public corporation organized and existing pursuant to the laws of the State of Alabama. Under the 30-year agreement, SEA will sell and deliver to the District and the District will purchase, specified quantities of natural gas at a market index price, less a specified discount. The initial gas delivery period (during which time the District is committed to purchase approximately 5,500,000 MMBtu of natural gas each year) began in November 2021 and will end in August 2028. That initial delivery period will be followed by one or more reset periods, during which a recalculated available discount will be applicable. If the available discount during any reset period is less than the minimum discount specified in the agreement, the District may elect not to take the contracted quantity of gas, in which event the District will have no rights or obligations to take or purchase any gas for the duration of that reset period.

After November 2028, the District may choose to switch the commodity being delivered from natural gas to electricity, in which event electricity will be delivered for the duration of the term.

After the initial discount period, the District's total potential commitment under this agreement is 126,320,000 MMBtu natural gas or 12,254,393 MWh of electricity.

In June 2022, the District entered into a second commodity purchase agreement with SEA. Under this 30-year agreement, SEA will sell and deliver to the District and the District will purchase, specified quantities of natural gas at a market index price, less a specified discount. The initial gas delivery period (during which time the District is committed to purchase approximately 3,620,000 MMBtu of natural gas each year) began in January 2023 and will end in June 2028. That initial delivery period will be followed by one or more reset periods, during which a recalculated available discount will be applicable. If the available discount during any reset period is less than the minimum discount specified in the agreement, the District may elect not to take the contracted quantity of gas, in which event the District will have no rights or obligations to take or purchase any gas for the duration of that reset period.

After June 2028, the District may choose to switch the commodity being delivered from natural gas to electricity, in which event electricity will be delivered for the duration of the term. After the initial discount period, the District's total potential commitment under this agreement is 90,020,000 MMBtu of natural gas or 10,851,011 MWh of electricity.

In March 2023, the District entered into a third commodity purchase agreement with SEA. Under this 30-year agreement, SEA will sell and deliver to the District, and the District will purchase specified quantities of natural gas at a market index price, less a specified discount. The initial gas delivery period (during which time the District is committed to purchase approximately 2,760,000 MMBtu of natural gas each year) will begin in July 2023 and will end in May 2029. That initial delivery period will be followed by one or more reset periods, during which a recalculated available discount will be applicable. If the available discount during any reset period is less than the minimum discount specified in the agreement, the District may elect to terminate the agreement or not to take the contracted quantity of gas, in which event the District will have no rights or obligations to take or purchase any gas for the duration of that reset period.

After July 2029, the District may choose to switch the commodity being delivered from natural gas to electricity, in which event electricity will be delivered for the duration of the term. After the initial discount period, the District's total potential commitment under this agreement is 72,010,000 MMBtu of natural gas or 7,018,383 MWh of electricity.

For all three commodity purchase transactions with SEA, the expense for the commodity delivered, net of discount, is recognized in total operating expenses in the Combined Statement of Net Revenues.

PVNGS Purchase Contracts

The District entered into certain contracts for the purchase of capacity of PVNGS, which is currently owned by certain lessors and leased to PNM. In addition, the District will acquire additional transmission capacity from PNM. The purchase is expected to be completed in fiscal year 2024, subject to regulatory approval, at a remaining cost of approximately \$2.0 million plus the cost of the associated nuclear fuel. The purchase of the additional interest in PVNGS will increase the District's ownership share of PVNGS to approximately 20%. The District paid \$17.7 million and \$46.9 million during fiscal year 2023 and 2022, respectively, for the purchase of capacity of PVNGS.

Gas Turbine Engine Purchase Contract

The District has entered into a contract for the purchase of eight gas turbine engines. The purchase is expected to be completed, and delivery is expected, in fiscal year 2024, at a remaining cost of approximately \$12.0 million, plus the cost of transportation services.

Nuclear Matters

Nuclear Insurance: Under existing law, public liability claims arising from a single nuclear incident are limited to \$13.6 billion. PVNGS participants insure for this potential liability through commercial insurance carriers to the maximum amount available, \$450.0 million, with the balance covered by an industrywide retrospective assessment program as required by the Price-Anderson Act. The maximum assessment per reactor per nuclear incident under the retrospective program is \$137.6 million, including a 5% surcharge applicable in certain circumstances. Based on the District's ownership share of PVNGS, the maximum potential assessment would be \$83.1 million, including the 5% surcharge.

PVNGS participants also maintain "all risk," including nuclear hazards, insurance for property damage to, and decontamination of, property at PVNGS in the aggregate amount of \$2.8 billion. The District also secured insurance against portions of any increased cost of generation or purchased power and any business interruption resulting from a sudden and unforeseen accidental 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.

Spent Nuclear Fuel: Under the Nuclear Waste Policy Act of 1982, the District was required to pay \$0.001 per kilowatt-hour on its share of net energy generation at PVNGS to the U.S. Department of Energy (DOE) through April 30, 2015 for the construction of a site for the storage of spent nuclear fuel. However, to date, for various reasons, the DOE has not constructed a storage site. Accordingly, Arizona Public Service Company, the operating agent for PVNGS, has constructed an on-site dry cask storage facility to receive and store PVNGS spent fuel. PVNGS has sufficient capacity at its on-site spent fuel storage installation to store all nuclear spent fuel until December 2027, the end of its first operating license period, and a portion of the future spent fuel during the period of extended operation, ending in December 2047. As a result of the DOE not constructing a storage site for the spent nuclear fuel, the DOE has made payments to nuclear facilities to reimburse a portion of the costs that have been incurred for fuel storage to date. SRP received \$2.5 million for fiscal year 2023 and \$2.1 million for fiscal year 2022. Effective May 15, 2014, the per-kilowatt-hour charge on energy generation at PVNGS was reduced to zero. A similar charge could be reinstated in the future.

The District's share of on-site interim storage at PVNGS is recovered through the District's base prices as a component of the system benefits charge. As of April 30, 2023 and 2022, the District's accrued spent fuel storage cost was \$24.6 million and \$20.7 million, respectively, and is included in deferred credits and other non-current liabilities on the accompanying Combined Balance Sheets.

Environmental Matters

SRP is subject to numerous legislative, administrative and regulatory requirements at the federal, state and local levels, as well as lawsuits relative to air quality, water quality, hazardous waste disposal and other environmental matters. Contingent losses and environmental liabilities are recorded when it is probable a loss has occurred and the amount of the loss can be reasonably estimated. When a range of the probable loss exists and no amount within the range is a better estimate than any other amount, SRP records a loss contingency at the minimum amount in the range, which is included in deferred credits and other non-current liabilities on the accompanying Combined Balance Sheets. As of April 30, 2023 and 2022, SRP had accrued liabilities of \$29.0 million and \$30.2 million, respectively, for environmental matters. The following topics highlight some of the major environmental compliance issues affecting the District.

Superfund: The United States and the State of Arizona have superfund programs to govern cleanup of groundwater contamination. Nineteen state superfund sites and six federal superfund sites targeting contamination are active within the Greater Phoenix metropolitan area. SRP has wells that are threatened or impacted by groundwater contamination located in sixteen of the nineteen state superfund sites and in two of the six federal superfund sites. The Association has agreed with other responsible parties to clean up one federal superfund site, and one District facility has been identified as a possible source of contamination for another federal superfund site. While SRP is unable at this time to predict the outcome of these superfund matters, it has recorded estimated liabilities to cover expected liabilities related to these issues.

Air quality: Compliance with air quality regulations designed to reduce emissions from fossil fuel power plants will increase the cost of, and add to the difficulty of, siting, constructing and operating electric generating units (EGUs). As a result of legislative and regulatory initiatives, the District has reduced emissions of mercury and other pollutants at its coal-fired power plants. The District continually assesses the risk of policy initiatives on its generation assets and develops contingency plans as necessary to comply with future laws and regulations relating to renewable energy and restricting greenhouse gas emissions.

EPA Carbon Regulations for Electric Generating Units – On July 8, 2019, the Environmental Protection Agency (EPA) published in the *Federal Register* the “Affordable Clean Energy” (ACE) rule that repeals and replaces the Clean Power Plan (CPP). Unlike the CPP, the ACE rule does not set state and tribal targets for carbon emission reductions. Instead, the rule requires states to set carbon emissions performance standards for existing coal-fired EGUs based on a revised determination that the “best system of emission reduction” (BSER) is application of heat rate improvement technologies. This rule is applicable to all coal-fired plants in which the District has an interest. Numerous states and cities and environmental groups challenged the ACE rule, and on January 19, 2021, the D.C. Circuit Court vacated and remanded the ACE rule to the EPA finding that ACE, as well as the repeal of the CPP, “hinged on a fundamental misconstruction of” Section 111(d). At the EPA’s request, the court ordered that it would withhold the issuance of the mandate with respect to the vacatur of the CPP repeal until the EPA responds to the court’s remand by promulgating a new Section 111(d) rule to regulate greenhouse gas emissions from EGUs. Multiple petitions for certiorari were filed with the U.S. Supreme Court asking the court to consider the extent of the EPA’s authority to regulate greenhouse gases at existing power plants. The Supreme Court granted certiorari and heard oral argument on February 28, 2022. In July 2022, the Supreme Court ruled that the EPA lacks the authority to regulate power plants by mandating the shifting of generation technology across generation fleets as required by the CPP.

On May 11, 2023, EPA issued a proposed new rule to: (i) revise the new source performance standards (NSPS) under Section 111(b) for GHG emissions from new fossil fuel-fired stationary combustion turbine EGUs; (ii) revise the NSPS for GHG emissions from fossil fuel-fired steam generating units that undertake a large modification; (iii) establish emission guidelines pursuant to Section 111(d) for GHG emissions from existing fossil fuel-fired steam generating EGUs, including coal-fired and oil/gas-fired steam generating EGUs; (iv) establish emission guidelines pursuant to Section 111(d) for GHG emissions from the largest, most frequently operated stationary combustion

turbines; and (v) repeal the ACE Rule. Public comments to the EPA's proposed rule are due by July 24, 2023. The District cannot predict the effects of this matter on its financial condition, net revenues, and cash flows at this time.

Mercury and Air Toxics Standards – In February 2012, EPA published the Mercury and Air Toxics Standards (MATS) rule, which established new emissions standards for trace metals, acid gases, mercury and organic compounds from existing and new coal- and oil-fired power plants under the Clean Air Act (CAA). The District complied with the MATS rule prior to the April 2016 deadline for compliance with the MATS mercury limit.

On May 22, 2020, EPA published in the Federal Register a final rule entitled “National Emission Standards for Hazardous Air Pollutants: Coal- and Oil-Fired Electric Utility Steam Generating Units – Reconsideration of Supplemental Finding and Residual Risk and Technology Review.” The rule rescinded the legal basis for the MATS rule and finalized a Risk and Technology Review (RTR) concluding that no further restrictions on EGU hazardous air pollutants (HAP) emissions were necessary. On June 19, 2020, numerous environmental, public health, and civil rights groups sued EPA challenging EPA's decision to rescind the agency's appropriate and necessary finding. On July 21, 2020, environmental groups filed a petition for review of EPA's final RTR. The groups challenge various aspects of the RTR as unlawful and/or arbitrary, including (i) EPA's decision to not set numeric emission limits for organic HAP; (ii) EPA's refusal to eliminate the “extended” startup period; (iii) the “new rationale” for excluding startup, shutdown, and malfunction (SSM) emissions from the risk analysis; and (iv) the multipath risk analysis. EPA filed a motion requesting the court hold the cases in abeyance pending EPA's review of the rule, and the court granted the motion on February 16, 2021. The District is monitoring the litigation.

On January 31, 2022, EPA proposed to reaffirm that it remains appropriate and necessary to regulate HAP emissions, including mercury, from power plants after considering cost. As part of the proposal, EPA stated the agency is also reviewing the 2020 RTR. Accordingly, the EPA solicited comment on the performance and cost of new or improved technologies that control HAP emissions, improved methods of operation, and risk-related information to further inform the agency's review of the MATS RTR. On February 15, 2023, EPA issued its rule restoring the agency's finding that it is “appropriate and necessary” to regulate power plants' air toxics. On April 24, 2023, EPA proposed to determine that the 2020 RTR was flawed and that the updated technology review requires certain changes to the MATS. For coal-fired EGUs, EPA is proposing to lower the emission limit for filterable particulate matter (fPM,) which serves as a surrogate for non-mercury HAP metals, from the current 0.030 lbs/MMBtu to 0.010 lbs/MMBtu, and possibly as low as 0.006 lbs/MMBtu. EPA also is proposing to require continuous emissions monitoring systems (CEMS) to demonstrate compliance with the fPM standard and eliminating the option to demonstrate compliance by conducting periodic stack testing or fPM continuous parameter monitoring systems. Affected EGUs would have to comply with the revised standards within three years of the effective date of the final rule. The District cannot predict the effects of this matter on its financial condition, net revenues, and cash flows at this time.

Regional Haze – Provisions of the EPA's Regional Haze Rule require emissions controls known as Best Available Retrofit Technology (BART) for coal-fired power plants and other industrial facilities that emit air pollutants that reduce visibility in Class I areas, such as national parks. The District has financial interests in several coal-fired power plants that underwent BART analysis during the first planning period of the Regional Haze Rule. The Arizona Department of Environmental Quality (ADEQ) conducted an initial analysis of Coronado Generating Station and Springerville Unit 4 as part of the State Implementation Plan (SIP) development process. The ADEQ has issued preliminary determinations that additional controls are not warranted for either facility. On August 15, 2022, the ADEQ submitted its SIP revision to EPA. EPA is currently reviewing the SIP revision to determine whether it meets the criteria for approval. The District is monitoring this activity and cannot predict the effects on its financial condition, net revenues and cash flows at this time.

Coronado Generating Station (CGS) – CGS is subject to source-specific terms as an alternative to BART under the Arizona Regional Haze SIP. The CGS SIP Revision consists of an interim operating strategy that is in effect from

December 5, 2017, to December 31, 2025, and a final operating strategy that would take effect on January 1, 2026. The interim operating strategy requires CGS to curtail Unit 1 for various time periods during certain winter months. The District is proceeding with a final operating strategy to install a Selective Catalytic Reduction (SCR) system on Unit 1. The District will couple the SCR operation on both units with continued seasonal curtailments of CGS' operation. Both units will retire no later than 2032.

Ozone National Ambient Air Quality Standards – Pursuant to the Clean Air Act (CAA), the EPA is required to review and, if appropriate and necessary, revise each of the established National Ambient Air Quality Standards (NAAQS) at five-year intervals. The 2008 ozone standard was set at 75 parts per billion (ppb) based on an eight-hour average.

On October 1, 2015, the EPA finalized revisions to the NAAQS and lowered both the primary and secondary ozone standard from the 2008 limit of 75 ppb down to 70 ppb (the 2015 ozone standard). On December 23, 2020, the EPA finalized the rule retaining the 70 ppb primary and secondary standards. In October 2021, the EPA indicated that it will reconsider its decision to retain the 2015 ozone standards. The District anticipates that the SIPs outlining controls to achieve the 2015 70 ppb standard will be in place in 2023. The District cannot predict the impact of the 2015 ozone standard and implementing controls on its operations, financial condition, net revenues and cash flows at this time.

PM_{2.5} National Ambient Air Quality Standards – On January 6, 2023, EPA announced a proposed decision to revise the primary annual PM_{2.5} standard from its current level of 12.0 ug/m³ to within the range of 9.0 to 10.0 ug/m³. EPA is not proposing to change the secondary annual PM_{2.5} standard, the primary and secondary 24-hour PM_{2.5} standards, or primary and secondary PM₁₀ standards. A change to the primary annual PM_{2.5} standard could result in additional areas within Arizona being designated as nonattainment with NAAQs. The District cannot predict the impact of a revised PM_{2.5} standard at this time.

The full significance of air quality standards and emissions reduction initiatives to the District in terms of costs and operational problems is difficult to predict. In addition, the cost of fossil fuel purchased by the District may increase and permit fees may increase significantly, resulting in potentially material increased costs to the District as well as reduced generation. The District cannot predict whether additional legislation or rules will be enacted that will affect the District's operations, the impact of any initiatives on the District and, if such laws or rules are enacted, what the costs to the District might be in the future because of such action.

Solid and Hazardous Waste Management: The District disposes of coal combustion residuals (CCRs,) such as fly ash, bottom ash and flue gas desulfurization sludge at CGS in a dry landfill and a wet surface impoundment. At NGS, disposal of CCRs was limited to a dry ash landfill; the District will close this facility as part of the NGS decommissioning process. The District also owns interests in joint participation plants, such as Four Corners, Craig Generating Station, Hayden Generating Station and Springerville Generating Station (Springerville), which dispose of CCRs in dry storage areas and in wet surface impoundments.

On October 19, 2015, federal criteria for management of CCRs as solid non-hazardous waste (CCR rule) became effective. The CCR rule is self-implementing and generally requires CCR disposal units to meet certain performance criteria. Units that do not meet the criteria must stop receiving CCRs and either retrofit to attain compliance or close. Costs to comply with this rule include costs for new groundwater monitoring wells, compliance monitoring and the eventual closure of residual ponds and storage areas.

On August 21, 2018, the United States Court of Appeals for the District of Columbia issued its ruling addressing challenges to the 2015 CCR rule promulgated by the EPA in *Utility Solid Waste Activities Group v. EPA* (USWAG decision). The decision vacated, as arbitrary and capricious, that portion of the CCR regulations that allowed existing unlined surface impoundments to continue operating unless and until the impoundments were shown to impact groundwater as determined by the groundwater protection standards.

The EPA significantly amended the CCR rule in 2020 to address the court's vacatur of the 2015 provisions. On August 28, 2020, the EPA published in the *Federal Register*, a final rule entitled "Hazardous and Solid Waste Management System: Disposal of Coal Combustion Residuals from Electric Utilities: A Holistic Approach to Closure Part A: Deadline to initiate Closure" (Part A rule). The Part A rule requires regulated entities to cease placing material in unlined surface impoundments on or before April 11, 2021.

On November 12, 2020, the EPA finalized a second rule entitled "Hazardous and Solid Waste Management System: Disposal of Coal Combustion Residuals from Electric Utilities: A Holistic Approach to Closure Part B: Alternate Demonstrations for Unlined Surface Impoundments (Part B rule)." The Part B rule establishes procedures to allow a limited number of facilities to continue using alternate liners at existing CCR surface impoundments. A facility seeking to make an alternate liner demonstration had to submit an application announcing its intent to submit an alternate liner demonstration with supporting documentation on or before November 30, 2020.

On November 25, 2020, the District submitted an application under the provisions of the Part B rule to make an alternate liner demonstration for the CGS wet surface impoundment. The District submitted its alternate liner demonstration on November 30, 2021. On January 11, 2022, the EPA notified the District that its application had been deemed complete. Under the Part B rule, the submission of a complete application tolls the April 11, 2021, cease receipt of waste deadline. On February 8, 2023, EPA published a proposed decision to deny the District's Part B application. The proposed decision states that, if EPA denies the District's application, the District must either: (1) submit an application to build a new facility in accordance with 40 C.F.R. § 257.103(f) no later than four months after EPA issues a final decision; or (2) cease using the CGS wet surface impoundment within 135 days of the date EPA issues the order, or such later date as EPA determines is necessary to address grid reliability.

The District believes EPA's proposed decision is wrong, arbitrary and capricious. Notably, EPA failed to consider the results of the District's extensive site characterization and hydrogeologic investigation conducted in 2021 and submitted to EPA over a year before EPA proposed to deny the District's Part B application. On April 10, 2023, the District submitted to the docket a comprehensive response supporting the District's Part B application. While the District believes it has submitted a robust application and alternate liner demonstration that meets the requirements of the Part B rule, the District cannot predict the outcome of this matter.

Endangered Species: Several species listed as threatened or endangered under the Endangered Species Act (ESA) have been discovered in and around reservoirs on the Salt and Verde rivers, as well as C.C. Cragin Reservoir, which is operated by the District. Potential ESA issues also exist along the Little Colorado River in the vicinity of CGS and Springerville. The District obtained Incidental Take Permits (ITPs) from the U.S. Fish and Wildlife Service (USFWS), which allow full operation of Roosevelt Dam on the Salt River and Horseshoe and Bartlett Dams on the Verde River. The ITPs and associated Habitat Conservation Plans (HCPs) identify the obligations, such as mitigation and wildlife monitoring, the District must undertake to comply with the ESA. The District has established trust funds to pay mitigation and monitoring expenses related to the implementation of both the Roosevelt HCP and Horseshoe-Bartlett HCP and believes it has recorded adequate reserves to cover its related obligations.

The USFWS finalized the listing of northern Mexican and narrow-headed garter snakes as threatened. On April 28, 2021, the USFWS designed 217 stream miles as critical habitat for the northern Mexican garter snake. On October 20, 2021, USFWS designated 447 stream miles in the Southwest as critical habitat for the narrow-headed garter snake. The District continues to assess the potential ESA liabilities regarding the northern Mexican and narrow-headed garter snakes. The District has initiated a process to amend the HCP and ITPs addressing operation of the Roosevelt Dam to address the northern Mexican garter snake. These species are included in the HCP and ITPs for operation of the Horseshoe and Bartlett dams.

Per- and Poly Fluoroalkyl Substances (PFAS): When necessary, the District supplements surface water from its Salt River and Verde River reservoirs with groundwater pumped from its extensive network of 270 groundwater wells. In cooperation with municipal and other partners, the District also operates and maintains two underground

storage facilities and one groundwater savings facility. Effluent from municipal water treatment plants is recharged into underlying aquifers through the District's underground storage facilities.

PFAS are a group of environmentally persistent, widespread man-made chemicals used in industrial applications and commercial household products that have received attention as emerging contaminants of concern in the environment. On June 15, 2022, EPA issued interim updated drinking water health advisories for perfluorooctanoic acid (PFOA) and perfluorooctane sulfonic acid (PFOS). The updated health advisories indicate that some negative health effects may occur with concentrations in drinking water above 0.004 parts per trillion (ppt) for PFOA and 0.02 ppt for PFOS. EPA's health advisories are non-enforceable and non-regulatory.

On August 26, 2022, EPA proposed to designate PFOA and PFAS, as hazardous substances under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). EPA is expected to issue a final rule in August 2023. EPA is also evaluating whether to list PFOA, PFOS, perfluorobutane sulfonate and similar chemicals as hazardous constituents under the Resource Conservation and Recovery Act.

On March 14, 2023, EPA announced the Proposed National Primary Drinking Water Regulation (NPDWR) (Proposed Rule) under the Safe Drinking Water Act (SDWA) for six per- and polyfluoroalkyl substances. The Proposed Rule would establish legally enforceable maximum contaminant levels (MCLs) for PFOA, PFOS, perfluorononanoic acid (PFNA), hexafluoropropylene oxide dimer acid (GenX Chemicals), perfluorohexane sulfonic acid (PFHxS) and perfluorobutane sulfonic acid (PFBS). EPA is proposing MCLs of 4.0 parts per trillion (ppt) for PFOA and PFOS and is proposing a Hazard Index ("HI") of 1.0 for PFHxS, HFPO-DA and its ammonium salt, PFNA, and PFBS and any mixture containing these substances. EPA explained that it is using the HI approach for these four PFAS compounds because it assesses health risks from simultaneous exposure to mixtures of related chemicals. Although EPA previously issued interim drinking water lifetime health advisories of 0.004 ppt for PFOA and 0.02 ppt for PFOS, EPA determined that an MCL of 4.0 ppt represents the lowest concentration that can be reliably and precisely quantified in "routine laboratory operating conditions."

The proposed limits would require public water systems to monitor for these chemicals and subsequently notify the public and reduce the levels of these PFAS compounds if levels exceed the proposed regulatory standards. In addition, these standards are likely to be taken into account in establishing cleanup levels at contaminated sites and may be incorporated into applicable state water quality standards. The deadline to submit comments on the proposed rule was May 30, 2023, and multiple industry groups, of which the District is a member, filed comments to the proposed rule on behalf of their respective members.

There are no state regulatory limits for PFAS in Arizona. The District is monitoring the regulatory developments regarding PFAS and may incur increased capital expenditures and maintenance costs as a result thereof. The District cannot predict the impact of these regulatory developments at this time.

Legal Matters

Water Rights: The District and the Association are parties to a state water-rights adjudication proceeding initiated in 1974 that encompasses the entire Gila River System. This proceeding is pending in the Superior Court for the State of Arizona, Maricopa County, and will eventually result in the determination of all conflicting rights to water from the Gila River and its tributaries, including the Salt and Verde rivers. The District and the Association are unable to predict the ultimate outcome of this proceeding.

In 1978, a water-rights adjudication was initiated in the Apache County Superior Court for the State of Arizona with regard to the Little Colorado River System and will eventually result in the determination of all conflicting rights to water from the Little Colorado River and its tributaries, including East Clear Creek, the location of C.C. Cragin Dam and Reservoir. The District is unable to predict the ultimate outcome of this proceeding but believes

an adequate water supply for CGS will remain available and that the rights to C.C. Cragin Dam and Reservoir will be confirmed.

2015 Price Process Litigation: On February 26, 2015, the Board concluded a public process by approving changes and adjustments to its retail electric price plans, including an overall average annual price increase of 3.9%, to be phased in beginning with the April 2015 billing cycle. This overall increase was composed of a 4.4% base increase and a 0.5% decrease to the Environmental Programs Cost Adjustment Factor.

In addition to other approved changes and adjustments, the Board approved a new price plan for residential customers who, after December 8, 2014, add solar or other technologies to generate some of their energy requirements (the E-27 Customer Generation Price Plan). The price plan includes a demand charge to better recover fixed costs related to the distributed generation customers' service facilities and their use of the grid, but also reduces the price such customers pay per kilowatt-hour for energy.

On February 22, 2019, four District customers who enrolled in the E-27 Customer Generation Price Plan filed a complaint in United States District Court for the District of Arizona, seeking class action status for all E-27 customers (the "Ellis Complaint"). The plaintiffs filed a First Amended Complaint on April 22, 2019. The Ellis Complaint alleges, among other things, that the District, by its adoption of the Customer Generation Price Plan, acted unlawfully by treating solar customers differently than non-solar customers. The suit asserts claims for unspecified damages and injunctive relief pursuant to federal and Arizona antitrust laws, price discrimination claims, equal protection claims, and an Arizona consumer fraud claim. The District moved to dismiss the First Amended Complaint on May 7, 2019. The court granted the District's motion to dismiss the lawsuit on various grounds, including dismissal of the claims for antitrust damages pursuant to the Local Government Antitrust Act. On February 20, 2020, plaintiffs filed a notice of appeal with the Ninth Circuit. The matter was briefed and oral argument was held on February 2, 2021. The Ninth Circuit issued an opinion on January 31, 2022, affirming the dismissal of six of nine claims and remanding the federal antitrust and equal protection claims to the Arizona District Court for further proceedings. The District filed a Renewed Motion to Dismiss as to the attempted monopolization and equal protection claims. On August 18, 2022, the Court granted the District's Renewed Motion to Dismiss and dismissed the equal protection and attempted monopolization claims, leaving only one claim remaining for injunctive relief with respect to the federal antitrust monopolization claim. This matter was amicably resolved by the parties and the case was dismissed on February 2, 2023.

Coolidge Expansion Project: On September 13, 2021, the Board of Directors for the District approved the construction of sixteen new gas-fired combustion turbines, known as the Coolidge Expansion Project (CEP). The CEP was intended to address a significant forecasted increase in electricity demand caused by Arizona's expanding commercial, residential and industrial sectors, while the District at the same time integrates an increasing amount of renewable—but intermittent—power sources like wind and solar. The District filed a siting application with the Arizona Corporation Commission (ACC) on December 13, 2021. In accordance with applicable statutory procedure, the District's application was first considered by the Arizona Power Plant and Transmission Line Siting Committee (Siting Committee) and then by the five Commissioners that comprise the ACC. The Siting Committee approved the CEP on February 15, 2022, following an eight-day evidentiary hearing. Thereafter, two intervenors, including the Randolph parties, sought review. On April 12, 2022, the ACC overturned the Siting Committee's decision and denied the application. The District requested reconsideration and rehearing of the ACC's decision, and, on June 6, 2022, the ACC denied the request for rehearing. On July 6, 2022, the District timely appealed the ACC's decision and filed a complaint in Maricopa County Superior Court (Superior Court). A two-day trial was held on January 4-5, 2023. On January 20, 2023, the Superior Court upheld the ACC's decision with respect to the CEP. On February 17, 2023, the District filed a timely Notice of Appeal with the Superior Court providing notice that the District is appealing the Superior Court's decision to the Arizona Court of Appeals. Refer to Note [16], SUBSEQUENT EVENTS, for additional information.

Other Litigation: In the normal course of business, SRP is exposed to various litigations or is a defendant in various litigation matters. In management’s opinion, except as otherwise noted herein, the ultimate resolution of these matters will not have a material adverse effect on SRP’s financial position or results of operations.

Other Matters

Self-insurance: SRP maintains various self-insurance retentions for certain casualty and property exposures. In addition, SRP has insurance coverage for amounts in excess of its self-insurance retention levels. SRP provides reserves based on management’s best estimate of claims, including incurred but not reported claims. In management’s opinion, the reserves established for these claims are adequate and any changes will not have a material adverse effect on SRP’s financial position or results of operations. SRP records the reserves in deferred credits and other non-current liabilities on the accompanying Combined Balance Sheets.

(16) SUBSEQUENT EVENTS:

On May 16, 2023, the District timely filed its brief with the Arizona Court of Appeals. On June 14, 2023, the District and the Randolph parties, one of the intervenors, reached a settlement with respect to those parties withdrawing their opposition to the District’s application for the CEP and therefore, also on June 14, 2023, the District filed a Motion with the ACC to rescind the earlier decision denying a Certificate of Environmental Compatibility (CEC) for the CEP and to request approval of an amended CEC for the CEP. On June 21, 2023, the ACC voted to approve the amended CEC for the CEP. In the meantime, the District has also requested that the Arizona Court of Appeals stay the appeal, which granted that request. While the ACC’s approval of the amended CEC represents an important milestone for the CEP, it is possible that one or more parties may request a rehearing of the ACC’s decision or file an appeal with respect to the ACC’s decision.

The terms of the settlement between the District and the Randolph parties include a commitment by the District to fund certain Randolph community programs and improvements contingent upon the commencement of construction of the CEP. The cost of the programs and improvements is estimated to be approximately \$23.8 million.



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