



A subsidiary of Pinnacle West Capital Corporation

Letter of Comment No: 5520  
File Reference: 1102-100

June 30, 2004

Ms. Suzanne Q. Bielstein  
Director of Major Projects  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, CT 06856-5116

RE: Proposed Statement of Financial Accounting Standards – Share-Based Payment,  
*an amendment of FASB Statements No. 123 and 95* (File Reference No. 1102-100)

Dear Ms. Bielstein,

We appreciate the opportunity to comment on the Proposed Statement of Financial Accounting Standards, Share-Based Payment, *an amendment of FASB Statements No. 123 and 95*. Arizona Public Service Company is a regulated public utility engaged in the generation, sale, and delivery of electricity and energy-related products in the western United States.

In general, we support the efforts of the FASB in developing financial reporting standards that will increase the comparability of financial statements worldwide; however, we have some concerns with the proposed amendment.

We believe that the fair value of an employee stock option at the vesting date is purely an estimate. As noted in Appendix B, Illustration 1 of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, in certain instances, both the Black-Scholes-Merton and binomial models produces the same fair value. We believe FASB should allow companies the flexibility to use a model which is appropriate to their facts and circumstances and considers costs and benefits of the available models. Therefore, we do not believe a specific model should be specified as preferable, nor should certain assumptions (i.e. volatility) be prescribed by the Board.

We do not believe that the attribution of compensation cost related to graded vesting under the proposed method most accurately reflects the cost of the service performed. We believe compensation cost of stock options should be treated consistently with other forms of compensation. To require accelerated expensing of the compensation cost as if stock options are individual awards would misrepresent the benefit a company receives from an employee's service. Additionally, if the proposed method were adopted, the additional complexity of record keeping for the awards would outweigh the benefit provided.

We strongly disagree with the proposed method of accounting for income taxes. We believe both tax benefit excesses and shortfalls that occur upon exercise of an

option should receive consistent accounting treatment. We believe any changes in value of a stock award between its grant date and exercise date should be attributed to the option holder and considered an equity transaction. Therefore, any increase or decrease in the tax benefit should be recorded as part of equity. Further, in order to determine whether an excess or shortfall is present upon exercise would require tracking by individual option which would create an undue burden in record keeping.

We believe the additional disclosure requirements are unnecessary to meet the disclosure objectives. We believe these requirements are satisfied by the current disclosure requirements of FASB Statement No. 123, as amended by FASB Statement No. 148. We believe that the original pronouncement provided sufficient disclosure for those companies that were accounting for stock options using the fair value method rather than the intrinsic method. If companies are required to adopt a fair value method, we believe the disclosure requirements prior to this amendment are sufficient.

We also disagree with the proposed treatment of classifying excess tax benefits as financing cash inflows in the cash flow statement. We believe this requirement would distort the statement of cash flows in that a non-cash item would be presented, which we believe is inconsistent with the purpose of FASB Statement No. 95. Further, this treatment would be inconsistent with other financing and investing activities, such as recognition of taxes paid in conjunction with a sale of a business. Under existing GAAP, taxes paid on the gain are reported as operating activities, whereas the cash flow from the gain is reported as financing activities.

We thank you again for the opportunity to comment on this issue.

Sincerely,

/s/ Chris N. Froggatt

Chris N. Froggatt  
Vice President & Controller  
Arizona Public Service Company  
400 North Fifth Street, P.O. Box 53999  
Phoenix, AZ 85072-3999