TUCSON ELECTRIC POWER CO
Form 10-K
February 27, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2012

OR

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

For the transition period from _____ to _____.

Commission File Number	Registrant; State of Incorporation; Address; and Telephone Number	IRS Employer Identification Number
1-13739	**UNS ENERGY CORPORATION** (An Arizona Corporation) 88 E. Broadway Boulevard Tucson, AZ 85701	86-0786732

(520) 571-4000

1-5924	**TUCSON ELECTRIC POWER COMPANY**	86-0062700
	(An Arizona Corporation)	
	88 E. Broadway Boulevard	
	Tucson, AZ 85701	
	(520) 571-4000	

Securities registered pursuant to Section 12(b) of the Exchange Act:

Registrant	**Title of Each Class**	**Name of Each Exchange on Which Registered**
UNS Energy Corporation	**Common Stock, no par value**	**New York Stock Exchange**

Securities registered pursuant to Section 12(g) of the Exchange Act:

Registrant	**Title of Each Class**	**Name of Each Exchange on Which Registered**
Tucson Electric Power Company	**Common Stock, without par value**	**N/A**

Indicate by check mark if the registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933.

UNS Energy Corporation	Yes x	No ¨
Tucson Electric Power Company	Yes ¨	No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 (Exchange Act).

UNS Energy Corporation	Yes ¨	No x
Tucson Electric Power Company	Yes ¨	No x

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

UNS Energy Corporation	Yes x	No ¨
Tucson Electric Power Company	Yes x	No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

UNS Energy Corporation	Yes x	No ¨
Tucson Electric Power Company	Yes x	No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of each registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

UNS Energy Corporation	Large Accelerated Filer x Smaller Reporting Company ¨	Accelerated Filer ¨	Non-accelerated filer ¨	
Tucson Electric Power Company	Large Accelerated Filer ¨ Smaller Reporting Company ¨	Accelerated Filer ¨	Non-accelerated filer x	

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

UNS Energy Corporation	Yes ¨	No x
Tucson Electric Power Company	Yes ¨	No x

The aggregate market value of UNS Energy Corporation voting Common Stock held by non-affiliates of the registrant was $1,574,040,179 based on the last reported sale price thereof on the consolidated tape on June 30, 2012.

At February 13, 2013, 41,386,469 shares of UNS Energy Corporation Common Stock, no par value (the only class of Common Stock), were outstanding.

At February 13, 2013, 32,139,434 shares of Tucson Electric Power Company s Common Stock, no par value, were outstanding, all of which were held by UNS Energy Corporation.

Tucson Electric Power Company meets the conditions set forth in General Instructions (I)(1)(a) and (b) on Form 10-K and is therefore filing this report with the reduced disclosure format.

Documents incorporated by reference: Specified portions of UNS Energy Corporation s Proxy Statement relating to the 2013 Annual Meeting of Shareholders are incorporated by reference into Part III.

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DEFINITIONS

The abbreviations and acronyms used in the 2012 Form 10-K are defined below:

1992 Mortgage	TEP s Indenture of Mortgage and Deed of Trust, dated as of December 1, 1992, to the Bank of New York Mellon, successor trustee, as supplemented
2010 TEP Reimbursement Agreement	Reimbursement Agreement dated December 14, 2010 among TEP as borrower and a financial institution
ACC	Arizona Corporation Commission
AFUDC	Allowance for Funds Used During Construction
AOCI	Accumulated Other Comprehensive Income
APS	Arizona Public Service Company
ARO	Asset Retirement Obligation
BART	Best Available Retrofit Technology
Base O&M	A non-GAAP financial measure that represents the fundamental level of operating and maintenance expense related to our business
Base Rates	The portion of TEP s and UNS Electric s Retail Rates attributed to generation, transmission, distribution costs, and customer charge; and UNS Gas delivery costs and customer charge. Base Rates exclude costs that are passed through to customers for fuel and purchased energy costs.
BHP	BHP Minerals International, Inc.
BMGS	Black Mountain Generating Station
Btu	British thermal unit(s)
Capacity	The ability to produce power; the most power a unit can produce or the maximum that can be taken under a contract; measured in megawatts
CC&N	Certificate of Convenience and Necessity
CCRs	Coal Combustion Residuals
Circuit Court	United States Court of Appeals
CO_2	Carbon Dioxide
Common Stock	UNS Energy s common stock, without par value
Company or UNS Energy	UNS Energy Corporation and its subsidiaries
Convertible Senior Notes	UNS Energy Corporation s 4.5% Convertible Senior Notes
Cooling Degree Days	An index used to measure the impact of weather on energy usage calculated by subtracting 75 from the average of the high and low daily temperatures
DSM	Demand Side Management
ECA	Environmental Compliance Adjustor
EEIP	Energy Efficiency Implementation Plan
Electric EE Standards	Electric Energy Efficiency Standards
Emission Allowance(s)	An allowance issued by the Environmental Protection Agency which permits emission of one ton of sulfur dioxide or one ton of nitrogen oxide; allowances can be bought and sold

Energy	The amount of power produced over a given period of time; measured in megawatt-hours
EPA	Environmental Protection Agency
EL Paso	El Paso Electric Company
EPNG	El Paso Natural Gas Company
EPS	Earnings Per Share
ESP	Electric Service Provider
FAA	Federal Arbitration Act
FERC	Federal Energy Regulatory Commission
Fixed CTC	Competition Transition Charge that was included in TEP s retail rate for the purpose of recovering TEP s Transition Recovery Asset; approximately $58 million was credited to customers through the PPFAC
Four Corners	Four Corners Generating Station
GAAP	Generally Accepted Accounting Principles
Gas EE Standards	Gas Utility Energy Efficiency Standards

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GHG	Greenhouse Gases
GWh	Gigawatt-hour(s)
Heating Degree Days	An index used to measure the impact of weather on energy usage calculated by subtracting the average of the high and low daily temperatures from 65
IDBs	Industrial development revenue or pollution control revenue bonds
IRS	Internal Revenue Service
kV	Kilovolt(s)
kWh	Kilowatt-hour(s)
LFCR	Lost Fixed Cost Recovery Mechanism
LIBOR	London Interbank Offered Rate
LOC	Letter of Credit
Long-Term Wholesale Margin Revenues	A non-GAAP measure that demonstrates the underlying profitability of TEP s long-term wholesale sales contracts
Luna	Luna Generating Station
Mark-to-Market Adjustments	Adjustments to forward energy sales and purchase contracts that are considered to be derivatives and are adjusted monthly by recording unrealized gains and losses to reflect the market prices at the end of each month
MATS	Mercury and Air Toxics Standards
Millennium	Millennium Energy Holdings, Inc., a wholly-owned subsidiary of UNS Energy
MMBtu	Million British Thermal Units
Mortgage Bonds	Mortgage Bonds issued under the 1992 Mortgage
MW	Megawatt(s)
MWh	Megawatt-hour(s)
Navajo	Navajo Generating Station
NERC	North American Electric Reliability Corporation
NO_x	Nitrogen oxide
NSP	Negotiated Sales Program
NTUA	Navajo Tribal Utility Authority
O&M	Operations and Maintenance
PBI	Performance Based Incentives
PGA	Purchased Gas Adjuster
PNM	Public Service Company of New Mexico
PNMR	PNM Resources, Incorporated, PNM s parent company
PPA	Power Purchase Agreement
PPFAC	Purchased Power and Fuel Adjustment Clause
PV	Photovoltaic
RCRA	Resource Conservation and Recovery Act
REC	Renewable Energy Credit
RES	Renewable Energy Standard and Tariff
Retail Margin Revenues	A non-GAAP financial measure that demonstrates the underlying revenue trend and performance of our core utility businesses
Retail Rates	Rates designed to allow a regulated utility an opportunity to recover its reasonable operating and capital costs and earn a return on its utility plant in service. Retail Rates include the recovery of fuel and purchased power costs, as well as other surcharges and adjustor

	mechanisms charged to retail customers.
Rules	Retail Electric Competition Rules established by the ACC in 1999
San Carlos	San Carlos Resources Inc., a wholly-owned subsidiary of TEP
San Juan	San Juan Generating Station
SERP	Supplemental Executive Retirement Plan
SCR	Selective Catalytic Reduction
SES	Southwest Energy Solutions, a wholly-owned subsidiary of Millennium
SO_2	Sulfur Dioxide
Springerville	Springerville Generating Station

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Springerville Coal Handling Facilities Leases	Leveraged lease arrangements relating to the coal handling facilities serving Springerville
Springerville Common Facilities	Facilities at Springerville used in common by all four Springerville units
Springerville Common Facilities Leases	Leveraged lease arrangements relating to an undivided one-half interest in certain Springerville Common Facilities
Springerville Unit 1	Unit 1 of the Springerville Generating Station
Springerville Unit 1 Leases	Leveraged lease arrangement relating to Springerville Unit 1 and an undivided one-half interest in certain Springerville Common Facilities
Springerville Unit 2	Unit 2 of the Springerville Generating Station
Springerville Unit 3	Unit 3 of the Springerville Generating Station
Springerville Unit 4	Unit 4 of the Springerville Generating Station
SRP	Salt River Project Agricultural Improvement and Power District
Sundt	H. Wilson Sundt Generating Station
Sundt Lease	The leveraged lease arrangement relating to Sundt Unit 4
Sundt Unit 4	Unit 4 of the H. Wilson Sundt Generating Station
SWG	Southwest Gas Corporation
TEP	Tucson Electric Power Company, the principal subsidiary of UNS Energy Corporation
TEP Credit Agreement	Second Amended and Restated Credit Agreement between TEP and a syndicate of banks, dated as of November 9, 2010 (as amended)
TEP Letter of Credit Facility	Letter of credit facility under the TEP Credit Agreement
TEP Revolving Credit Facility	Revolving credit facility under the TEP Credit Agreement
Therm	A unit of heating value equivalent to 100,000 Btus
Transwestern	Transwestern Pipeline Company
Tri-State	Tri-State Generation and Transmission Association, Inc.
UED	UniSource Energy Development Company, a wholly-owned subsidiary of UNS Energy Corporation
UES	UniSource Energy Services, Inc., an intermediate holding company established to own UNS Gas and UNS Electric
UNS Credit Agreement	Second Amended and Restated Credit Agreement between UNS Energy and a syndicate of banks, dated as of November 9, 2010 (as amended)
UNS Energy	UNS Energy Corporation (formerly known as UniSource Energy Corporation)
UNS Electric	UNS Electric, Inc., a wholly-owned subsidiary of UES
UNS Electric Term Loan	Four-year $30 million term loan agreement dated as of August 10, 2011
UNS Gas	UNS Gas, Inc., a wholly-owned subsidiary of UES
UNS Gas/UNS Electric Revolver	Revolving credit facility under the Second Amended and Restated Credit Agreement among UNS Gas and UNS Electric as borrowers, and UES as guarantor, and a syndicate of banks, dated as of November 9, 2010 (as amended)
Valencia	Valencia power plant owned by UNS Electric
VEBA	Voluntary Employee Beneficiary Association
WAPA	Western Area Power Administration

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PART I

This combined Form 10-K is being filed separately by UNS Energy Corporation (UNS Energy) and Tucson Electric Power Company (TEP) (collectively, the Registrants). Information contained herein relating to any individual registrant is filed by such registrant on its own behalf. TEP does not make any representation as to information relating to any other subsidiary of UNS Energy.

This Annual Report on Form 10-K contains forward-looking statements as defined by the Private Securities Litigation Reform Act of 1995. You should read forward-looking statements together with the cautionary statements and important factors included elsewhere in this Form 10-K (See *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Safe Harbor for Forward-Looking Statements*). Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions. Forward-looking statements are not statements of historical facts. Forward-looking statements may be identified by the use of words such as anticipates, estimates, expects, intends, plans, predicts, projects, and similar expressions. We express our expecta beliefs, and projections in good faith and believe them to have a reasonable basis. However, we make no assurances that management s expectations, beliefs, or projections will be achieved or accomplished. In addition, UNS Energy and TEP disclaim any obligation to update any forward-looking statements to reflect events or circumstances after the date of this report.

ITEM 1. BUSINESS

OVERVIEW OF CONSOLIDATED BUSINESS

UNS Energy Corporation (UNS Energy), formerly UniSource Energy Corporation, is a utility services holding company engaged, through its subsidiaries, in the electric generation and energy delivery business. Each of UNS Energy s subsidiaries is a separate legal entity with its own assets and liabilities. UNS Energy owns 100% of Tucson Electric Power Company (TEP), UniSource Energy Services, Inc. (UES), Millennium Energy Holdings, Inc. (Millennium), and UniSource Energy Development Company (UED).

TEP is a regulated public utility and UNS Energy s largest operating subsidiary, representing approximately 84% of UNS Energy s total assets as of December 31, 2012. TEP generates, transmits and distributes electricity to approximately 406,000 retail electric customers in a 1,155 square mile area in southeastern Arizona. TEP also sells electricity to other utilities and power marketing entities, located primarily in the western United States. In addition, TEP operates Springerville Generating Station (Springerville) Unit 3 on behalf of Tri-State Generation and Transmission Association, Inc. (Tri-State) and Springerville Unit 4 on behalf of Salt River Project Agriculture Improvement and Power District (SRP).

UES holds the common stock of two regulated public utilities, UNS Gas, Inc. (UNS Gas) and UNS Electric, Inc. (UNS Electric). UNS Gas is a regulated gas distribution company, which services approximately 149,000 retail customers in Mohave, Yavapai, Coconino, and Navajo counties in northern Arizona, as well as in Santa Cruz County in southern Arizona. UNS Electric is a regulated public utility, which generates, transmits and distributes electricity to approximately 92,000 retail customers in Mohave and Santa Cruz counties.

UED and Millennium s investments in unregulated businesses represent less than 1% of UNS Energy s assets as of December 31, 2012.

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BUSINESS SEGMENT CONTRIBUTIONS

The table below shows the contributions to our consolidated after-tax earnings by our three business segments.

	2012	2011	2010
	-Millions of Dollars-		
TEP	$ 65	$ 85	$ 108
UNS Gas	9	10	9
UNS Electric	17	18	15
Other Non-Reportable Segments and Adjustments[(1)]		(3)	(19)
Consolidated Net Income	$ 91	$ 110	$ 113

(1) Includes: UNS Energy parent company expenses, Millennium, UED, and intercompany eliminations.

See Note 3 for additional financial information regarding our business segments.

References in this report to we and our are to UNS Energy and its subsidiaries, collectively.

Rates and Regulation of TEP, UNS Gas, and UNS Electric

The Arizona Corporation Commission (ACC) regulates portions of TEP, UNS Gas, and UNS Electric s utility accounting practices and energy rates. The ACC has authority over rates charged to retail customers, the issuance of securities, and transactions with affiliated parties. Our regulated utility rates for retail electric and natural gas service are determined on a cost of service basis. Retail Rates are designed to provide, after recovery of allowable operating expenses, an opportunity for our utility businesses to earn a reasonable return on rate base. Rate base is generally determined by reference to the original cost (net of depreciation) of utility plant in service to the extent deemed used and useful, and to various adjustments for deferred taxes and other items, plus a working capital component. Over time, additions to utility plant in service increase rate base while depreciation and retirements of utility plant reduce rate base.

The rates charged to retail customers by TEP, UNS Gas, and UNS Electric also include pass-through mechanisms that allow each utility to recover the actual costs of its fuel, transmission, and energy purchases.

The Federal Energy Regulatory Commission (FERC) regulates the terms and prices of transmission services and wholesale electricity sales, wholesale transport and purchases of natural gas, and portions of our accounting practices. TEP and UNS Electric have FERC tariffs to sell power at market-based rates.

TEP

TEP was incorporated in the State of Arizona in 1963. TEP is the principal operating subsidiary of UNS Energy. In 2012, TEP s electric utility operations contributed 78% of UNS Energy s operating revenues and comprised 84% of its assets.

SERVICE AREA AND CUSTOMERS

TEP is a vertically integrated utility that provides regulated electric service to approximately 406,000 retail customers in southeastern Arizona. TEP s service territory covers 1,155 square miles and includes a population of approximately one million people in the greater Tucson metropolitan area in Pima County, as well as parts of Cochise County. TEP also sells electricity to other entities in the western United States.

Retail Customers

TEP provides electric utility service to a diverse group of residential, commercial, industrial, and public sector customers. Major industries served include copper mining, cement manufacturing, defense, health care, education, military bases, and other governmental entities. TEP s

retail sales are influenced by several factors, including economic conditions, seasonal weather patterns, demand side management (DSM) initiatives and the increasing use of energy efficient products, and opportunities for customers to generate their own electricity.

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Customer Base

The table below shows the percentage distribution of TEP s energy sales by major customer class over the last three years. In 2013, the retail energy consumption by customer class is expected to be similar to the historical distribution.

	2012	2011	2010
Residential	41%	42%	42%
Commercial	21%	21%	21%
Non-mining Industrial	23%	23%	23%
Mining	12%	11%	12%
Public Authority	3%	3%	2%

Local, regional, and national economic factors can impact the growth in the number of customers in TEP s service territory. In 2012, 2011, and 2010, TEP s average number of retail customers increased by less than 1% in each year.

We expect the number of TEP s retail customers to increase at a rate of less than 1% in 2013 and 2014.

Two of TEP s largest retail customers are in the copper mining industry. TEP s kilowatt-hour (kWh) sales to mining customers depend on a variety of factors including the market price of copper, the electricity rate paid by mining customers, and the mines potential development of their own electric generation resources. TEP s kWh sales to mining customers increased by 0.9% in 2012 and 0.3% in 2011 as a result of increased production due to high copper prices.

Retail Sales Volumes

During the past three years, economic conditions and state requirements for energy efficiency and distributed generation have negatively affected retail electricity sales. TEP s retail sales volumes in 2012 were approximately 9,265 Gigawatt-hours (GWh) or 1.1% below 2009.

Energy Service Providers

Although the Retail Electric Competition Rules established by the ACC in 1999 (Rules) contemplated that TEP s retail customers may be eligible to choose an alternative energy service provider (ESP), portions of those Rules have been invalidated by the Arizona courts and there are no ESPs currently authorized to provide alternative retail electric service to TEP s customers. See *Rates and Regulation,* below for more information regarding the status of retail competition in Arizona.

Wholesale Business

TEP s electric utility operations include the wholesale marketing of electricity to other utilities and power marketers. Wholesale sales transactions are made on both a firm and interruptible basis. A firm contract requires TEP to supply power on demand (except under limited emergency circumstances), while an interruptible contract allows TEP to stop supplying power under defined conditions. See *Generating and Other Resources, Purchases and Interconnections*, below.

Generally, TEP commits to future sales based on expected excess generating capability, forward prices, and generation costs, using a diversified portfolio approach to provide a balance between long-term, mid-term, and spot energy sales. TEP s wholesale sales consist primarily of two types of sales:

Long-Term Sales

Long-term wholesale sales contracts cover periods of more than one year. TEP typically uses its own generation to serve the requirements of its long-term wholesale customers. TEP s long-term contracts are described below:

From January 1, 2012 through the end of the contract in May 2016, Salt River Project Agriculture Improvement and Power District (SRP) is required to purchase 500,000 MWh of on-peak energy per year. TEP does not receive a demand charge and the price of energy is based on a discount to the Palo Verde Market Index. Prior to June 1, 2011, TEP received an annual demand charge of approximately $22 million.

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TEP s contract with the Navajo Tribal Utility Authority (NTUA) expires in December 2015. TEP serves the portion of NTUA s load that is not served by the authority s allocation of federal hydroelectric power. Over the last three years, sales to NTUA averaged 225,000 MWh per year. Since 2010, the price of 50% of the MWh sales to NTUA from June to September has been based on the Palo Verde Market Index. In 2012, approximately 13% of the total energy sold to NTUA was priced based on the Palo Verde Market Index. The remaining power sales occur at a fixed price under TEP s contract with NTUA.

TEP s 2 MW contract with the Tohono O odham Utility Authority expires in 2014.

Short-Term Sales

Forward contracts commit TEP to sell a specified amount of capacity or energy at a specified price over a given period of time, typically for one-month, three-month, or one-year periods. TEP also engages in short-term sales by selling energy in the daily or hourly markets at fluctuating spot market prices and making other non-firm energy sales. All revenues from short-term wholesale sales offset fuel and purchased power costs and are passed through to TEP s retail customers. TEP uses short-term wholesale sales as part of its hedging strategy to reduce customer exposure to fluctuating power prices. See *Rates and Regulation,* below.

See *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power Company, Factors Affecting Results of Operations,* for additional discussion of TEP s wholesale marketing activities.

GENERATING AND OTHER RESOURCES

At December 31, 2012, TEP owned or leased 2,267 MW of net generating capability, as set forth in the following table:

Generating Source	Unit No.	Location	Date In Service	Resource Type	Net Capability MW	Operating Agent	TEP %	s Share MW
Springerville Station[1]	1	Springerville, AZ	1985	Coal	401	TEP	100.0	401
Springerville Station	2	Springerville, AZ	1990	Coal	403	TEP	100.0	403
San Juan Station	1	Farmington, NM	1976	Coal	340	PNM	50.0	170
San Juan Station	2	Farmington, NM	1973	Coal	340	PNM	50.0	170
Navajo Station	1	Page, AZ	1974	Coal	750	SRP	7.5	56
Navajo Station	2	Page, AZ	1975	Coal	750	SRP	7.5	56
Navajo Station	3	Page, AZ	1976	Coal	750	SRP	7.5	56
Four Corners Station	4	Farmington, NM	1969	Coal	784	APS	7.0	55
Four Corners Station	5	Farmington, NM	1970	Coal	784	APS	7.0	55
Luna Generating Station	1	Deming, NM	2006	Gas	555	PNM	33.3	185
Sundt Station	1	Tucson, AZ	1958	Gas/Oil	81	TEP	100.0	81
Sundt Station	2	Tucson, AZ	1960	Gas/Oil	81	TEP	100.0	81
Sundt Station	3	Tucson, AZ	1962	Gas/Oil	104	TEP	100.0	104
Sundt Station	4	Tucson, AZ	1967	Coal/Gas	156	TEP	100.0	156
Sundt Internal Combustion Turbines		Tucson, AZ	1972-1973	Gas/Oil	50	TEP	100.0	50
DeMoss Petrie		Tucson, AZ	1972	Gas/Oil	75	TEP	100.0	75
North Loop		Tucson, AZ	2001	Gas	95	TEP	100.0	95
Springerville Solar Station		Springerville, AZ	2002-2010	Solar	6	TEP	100.0	6
Tucson Solar Projects		Tucson, AZ	2010-2012	Solar	12	TEP	100.0	12
Total TEP Capacity [2]								2,267

(1) Leased asset as of December 31, 2012.

(2) Excludes 683 MW of additional resources, which consist of certain capacity purchases and interruptible retail load. At December 31, 2012, total owned capacity was 1,866 MW and leased capacity was 401 MW.

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Springerville Generating Station

TEP currently owns a 14% undivided interest in Unit 1 of the Springerville Generating Station (Springerville Unit 1) and the remainder is leased by TEP. Unit 2 of the Springerville Generating Station (Springerville Unit 2) is owned by San Carlos Resources, Inc. (San Carlos), a wholly-owned subsidiary of TEP. TEP s other interests in the Springerville Generating Station (Springerville) include leasehold interests in the Springerville Coal Handling Facilities and the facilities at Springerville used in common by all four Springerville units (Springerville Common Facilities).

Springerville Unit 1 Leases

The terms of the leveraged lease arrangement relating to Springerville Unit 1 and an undivided one-half interest in certain Springerville Common Facilities (Springerville Unit 1 Leases), expire in 2015 but have optional fair market value renewal and purchase provisions. In 1985, TEP sold and leased back the remaining 50% interest in the Springerville Common Facilities.

In December 2011, TEP and the owner participants of the Springerville Unit 1 Leases completed a formal appraisal procedure to determine the fair market value purchase price. The formal appraisal process was completed in accordance with the Springerville Unit 1 lease agreements. The purchase price was determined to be $478 per kW of capacity, based on a continuous capacity rating of 387 MW. TEP has until September 1, 2013 to give notice that it will exercise its purchase option, with the purchase occurring in January 2015. TEP can choose to exercise this option to purchase any or all of the lease interests not currently owned by TEP. If TEP chooses to purchase all of the remaining interests in Springerville Unit 1 from the owner participants, the aggregate purchase price would be $159 million. See *Item 3. Legal Proceedings*, *Springerville Unit 1 Appraisal.*

Springerville Common Facilities Leases

The leveraged lease arrangements relating to an undivided one-half interest in certain Springerville Common Facilities (Springerville Common Facilities Leases), which expire in 2017 and 2021, have optional fair market value renewal options as well as a fixed-price purchase provision. The fixed prices to acquire the leased interests in the Springerville Common Facilities are $38 million in 2017 and $68 million in 2021.

Springerville Coal Handling Facilities Lease

In 1984, TEP sold and leased back the Springerville Coal Handling Facilities. Since entering the lease, TEP purchased a 13% ownership interest in the Springerville Coal Handling Facilities. The terms of the Springerville Coal Handling Facilities Leases expire in April 2015 but have optional fixed-rate renewal options if certain conditions are satisfied as well as a fixed-price purchase provision of $120 million.

See Note 6 and *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power Company, Liquidity and Capital Resources, Contractual Obligations*, for more information regarding the Springerville leases.

Sundt Generating Station

The H. Wilson Sundt Generating Station (Sundt) and the internal combustion turbines located in Tucson are designated as must-run generation facilities. Must-run generation units are required to run in certain circumstances to maintain distribution system reliability and to meet local load requirements.

In 2010, TEP purchased 100% of the equity interest in the Sundt Unit 4 lease for approximately $51 million, redeemed the outstanding Sundt Unit 4 lease debt of $5 million, and terminated the lease agreement.

Renewable Energy Resources

Owned Resources

As of December 31, 2012, TEP owned 18 MW of photovoltaic (PV) solar generating capacity. The Springerville solar system, which is located near the Springerville Generating Station, has a total capacity of 6 MW. TEP s remaining 12 MW of PV solar generating capacity is located in the City of Tucson.

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Power Purchase Agreements

In order to meet the ACC s renewable energy requirements, TEP has power purchase agreements (PPAs) for 125 MW of capacity from solar resources, 50 MW of capacity from wind resources and 2 MW of capacity from a landfill gas generation plant. As of December 31, 2012, approximately 74 MW of contracted solar resources and 50 MW of contracted wind resources were operational. The remaining resources are expected to be developed over the next several years. The solar PPAs contain options that would allow TEP to purchase all or part of the related project at a future period. See *Rates and Regulation, Renewable Energy Standard and Tariff* below for more information.

Purchases and Interconnections

TEP purchases power from other utilities and power marketers. TEP may enter into contracts: (a) to purchase energy under long-term contracts to serve retail load and long-term wholesale contracts, (b) to purchase capacity or energy during periods of planned outages or for peak summer load conditions, and (c) to purchase energy for resale to certain wholesale customers under load and resource management agreements.

TEP typically uses generation from its gas-fired units, supplemented by power purchases, to meet the summer peak demands of its retail customers. Some of these PPAs are price-indexed to natural gas prices. Due to its increasing seasonal gas and purchased power usage, TEP hedges a portion of its total natural gas exposure with fixed price contracts for a maximum of three years. TEP also purchases energy in the daily and hourly markets to meet higher than anticipated demands, to cover unplanned generation outages, or when doing so is more economical than generating its own energy.

TEP is a member of a regional reserve-sharing organization and has reliability and power sharing relationships with other utilities. These relationships allow TEP to call upon other utilities during emergencies, such as plant outages and system disturbances, and reduce the amount of reserves TEP is required to carry.

As a result of the Energy Policy Act of 2005, owners and operators of bulk power transmission systems, including TEP, are subject to mandatory reliability standards that are developed and enforced by the North American Electric Reliability Corporation (NERC) and subject to the oversight of the FERC. TEP periodically reviews its operating policies and procedures to ensure continued compliance with these standards.

Springerville Units 3 and 4

Springerville Units 3 and 4 are each approximately 400 MW coal-fired generating facilities that are operated, but not owned by TEP. These facilities are located at the same site as TEP s Springerville Units 1 and 2. The owners of Springerville Units 3 and 4 compensate TEP for operating the facilities and pay an allocated portion of the fixed costs related to the Springerville Common Facilities and Coal Handling Facilities. See *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power Company, Factors Affecting Results of Operations, Springerville Units 3 and 4*.

Peak Demand and Resources

Peak Demand	2012	2011	2010	2009	2008
			-MW-		
Retail Customers	2,290	2,334	2,333	2,354	2,376
Firm Sales to Other Utilities	286	322	340	385	394
Coincident Peak Demand (A)	2,576	2,656	2,673	2,739	2,770
Total Generating Resources	2,267	2,262	2,245	2,229	2,204
Other Resources [(1)]	683	1,009	799	781	966
Total TEP Resources (B)	2,950	3,271	3,044	3,010	3,170
Total Margin (B) (A)	374	615	371	271	400
Reserve Margin (% of Coincident Peak Demand)	15%	23%	14%	10%	14%

(1) Other Resources include firm power purchases and interruptible retail and wholesale loads. Additional firm power purchases were made in 2009 and 2010 to displace more expensive owned gas generation.

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Peak demand occurs during the summer months due to the cooling requirements of TEP s retail customers. Retail peak demand varies from year-to-year due to weather, economic conditions, and other factors. TEP s retail peak demand declined over the period of 2008 to 2012 due primarily to weak economic conditions and the implementation of energy efficiency programs.

The chart above shows the relationship over a five-year period between TEP s peak demand and its energy resources. TEP s total margin is the difference between total energy resources and coincident peak demand, and the reserve margin is the ratio of margin to coincident peak demand. TEP s reserve margin in 2012 was in compliance with reliability criteria set forth by the Western Electricity Coordinating Council, a regional council of NERC.

Forecasted retail peak demand for 2013 is 2,243 MW, compared with actual peak demand of 2,290 MW in 2012 when Cooling Degree Days exceeded the ten-year average by 4.9%. TEP s 2013 estimated retail peak demand is based on normal weather patterns. TEP believes existing generation capacity and power purchase agreements are sufficient to meet expected demand in 2013.

Future Generating Resources

TEP will add generating resources and/or transmission import capability to meet forecasted retail and firm wholesale load. TEP expects to add approximately 65 MW of new solar PV resources in 2013.

FUEL SUPPLY

Fuel Summary

Fuel cost and usage information is provided below:

	Average Cost per MMBtu Consumed			Percentage of Total Btu Consumed		
	2012	2011	2010	2012	2011	2010
Coal	$ 2.44	$ 2.42	$ 2.23	88%	92%	90%
Gas	$ 3.92	$ 5.20	$ 4.69	12%	8%	10%
All Fuels	$ 2.63	$ 2.65	$ 2.47	100%	100%	100%

Coal

TEP s principal fuel for electric generation is low-sulfur, bituminous or sub-bituminous coal from mines in Arizona, New Mexico, and Colorado. More than 90% of TEP s coal supply is purchased under long-term contracts, which results in more predictable prices. The average cost per ton of coal, including transportation, was $45.84 in 2012, $46.64 in 2011, and $41.99 in 2010.

Station	Coal Supplier	2012 Coal Consumption (tons in 000 s)	Contract Expiration	Avg. Sulfur Content	Coal Obtained From[1]
Springerville	Peabody Coalsales	3,287	2020	0.9%	Lee Ranch Coal Co.
Four Corners	BHP Billiton	400	2016	0.8%	Navajo Indian Tribe
San Juan	San Juan Coal Co.	1,098	2017	0.8%	Federal and State Agencies
Navajo	Peabody Coalsales	475	2019	0.4%	Navajo and Hopi Indian Tribes

(1) Substantially all of the suppliers mining leases extend at least as long as coal is being mined in economic quantities.

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TEP Operated Generating Facilities

TEP is the operator, and sole owner (or lessee), of the Springerville Units 1 and 2 and Sundt Unit 4. The coal supplies for Springerville Units 1 and 2 are transported approximately 200 miles by railroad from northwestern New Mexico. TEP expects coal reserves to be sufficient to supply the estimated requirements for Springerville Units 1 and 2 for their presently estimated remaining lives.

The coal supplies for Sundt Unit 4 are transported approximately 1,300 miles by railroad from Colorado. Prior to 2010, Sundt Unit 4 was predominantly fueled by coal; however, the generating station also can be operated with natural gas. Both fuels are combined with methane, a renewable energy resource, piped in from a nearby landfill. Since 2010, TEP has fueled Sundt Unit 4 with both coal and natural gas depending on which resource is most economic. In 2013, TEP expects to fuel Sundt Unit 4 with coal from inventory. See Note 4 for more information.

Generating Facilities Operated by Others

TEP also participates in jointly-owned coal-fired generating facilities at the Four Corners Generating Station (Four Corners), the Navajo Generating Station (Navajo), and the San Juan Generating Station (San Juan). Four Corners, which is operated by Arizona Public Service (APS), and San Juan, which is operated by Public Service Company of New Mexico (PNM), are mine-mouth generating stations located adjacent to the coal reserves. Navajo, which is operated by SRP, obtains its coal supply from a nearby coal mine and a dedicated rail delivery system. The coal supplies are under long-term contracts administered by the operating agents. TEP expects coal reserves available to these three jointly-owned generating facilities to be sufficient for the remaining presently estimated lives of the stations.

Natural Gas Supply

TEP typically uses generation from its facilities fueled by natural gas, in addition to energy from its coal-fired facilities and purchased power, to meet the summer peak demands of its retail customers and local reliability needs. TEP purchases gas from Southwest Gas Corporation under a retail tariff for North Loop s 95 MW of internal combustion turbines and receives distribution service under a transportation agreement for DeMoss Petrie, a 75 MW internal combustion turbine. TEP purchases capacity from El Paso Natural Gas Company (EPNG) for transportation from the San Juan and Permian Basins to its Sundt plant under a contract that expires in April 2013, with right-of-first-refusal for continuation thereafter. TEP also buys gas from third-party suppliers for Sundt and DeMoss Petrie.

TEP purchases gas transportation for Luna Generating Station (Luna) from EPNG from the Permian Basin to the plant site under an agreement effective through January 2017, with right-of-first-refusal for continuation thereafter. TEP purchases gas for its share of Luna from various suppliers in the Permian Basin region.

TRANSMISSION ACCESS

TEP has transmission access and power transaction arrangements with over 120 electric systems or suppliers. TEP also has various ongoing projects that are designed to increase access to the regional wholesale energy market and improve the reliability, capacity and efficiency of its existing transmission and distribution systems.

TEP is participating in the continuation of the 500 kV transmission line from the Pinal West substation to the Pinal Central substation. TEP has obtained ACC approval to build a 40-mile 500-kV transmission line from the Pinal Central substation to the Tortolita substation northwest of Tucson to further enhance its ability to access the region s energy resources. TEP expects the transmission lines to be in service in 2016. As a result of these high-voltage transmission additions, TEP expects that its ability to import energy into its service territory would increase by at least 250 MW.

Tucson to Nogales Transmission Line

TEP and UNS Electric are parties to a project development agreement for the joint construction of a 60-mile transmission line from Tucson, Arizona to Nogales, Arizona. This project was initiated in response to an order by the ACC to UNS Electric to improve the reliability of electric service in Nogales. TEP had previously capitalized $11 million related to the project, including $2 million to secure land and land rights. UNS Electric had previously capitalized $0.4 million related to the project.

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TEP and UNS Electric expect to abandon the project based on the cost of the proposed 345-kV line, the difficulty in reaching agreement with the Forest Service on a path for the line, and concurrence by the ACC of recent transmission plans filed by TEP and UNS Electric supporting the elimination of this project. In TEP s pending rate case proceeding before the ACC, TEP entered into a proposed settlement agreement in which it agrees to seek recovery of the project costs from FERC before seeking rate recovery from the ACC. In the fourth quarter of 2012, TEP and UNS Electric wrote off a portion of the capitalized costs believed not probable of recovery and recorded a regulatory asset for the balance deemed probable of recovery. TEP and UNS Electric believe it is probable that we will recover at least $5 million and $0.2 million, respectively, of costs incurred through 2012. See Note 4 and see *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power, Factors Affecting Results of Operations, 2012 TEP Rate Case*, for more information.

RATES AND REGULATION

2012 TEP Rate Case

In July 2012, TEP filed an application for a base rate increase with the ACC. See *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power, Factors Affecting Results of Operations, 2012 TEP Rate Case*, for more information.

Purchased Power and Fuel Adjustment Clause

The Purchased Power and Fuel Adjustment Clause (PPFAC) allows TEP to recover its fuel, transmission, and purchased power costs, including demand charges, and the prudent costs of contracts for hedging fuel and purchased power costs from its retail customers. The PPFAC consists of a forward component and a true-up component.

The forward component is updated on April 1 of each year. The forward component is based on the forecasted fuel and purchased power costs for the 12-month period from April 1 to March 31 of the following year.

The true-up component will reconcile any over/under collected amounts from the preceding 12-month period and will be credited to or recovered from customers in the subsequent year.

As part of the reconciliation of fuel and purchased power costs and PPFAC revenues, TEP credits, among other things, 100% of short-term wholesale revenues against the recoverable costs.

In March 2012, the ACC approved a PPFAC rate of 0.77 cents per kWh effective April 2012 to recover $77 million of under-collected fuel and purchased power costs. At December 31, 2012, TEP had under-collected fuel and purchased power costs on a billed-to-customer basis of $12 million.

A proposed settlement agreement in TEP s pending rate case proceeding includes certain modifications to TEP s PPFAC. In February 2013, TEP filed a request with the ACC to defer the effective date of resetting the PPFAC until the effective date of new rates in TEP s pending rate case. This request is consistent with a provision of the settlement agreement. TEP cannot predict if or when the ACC will respond to its request. See *Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Tucson Electric Power, Factors Affecting Results of Operations, 2012 TEP Rate Case*, *PPFAC Modifications*, for more information.

Renewable Energy Standard and Tariff

The ACC s Renewable Energy Standard (RES) requires TEP, UNS Electric, and other affected utilities to increase their use of renewable energy each year until it represents at least 15% of their total annual retail energy requirements in 2025. Affected utilities must file annual RES implementation plans for review and approval by the ACC. The approved cost of carrying out those plans is recovered from retail customers through the RES surcharge. Any RES surcharge collections above or below the costs incurred to implement the plans are deferred and reflected in TEP s financial statements as a regulatory asset or liability.

In 2010, the ACC approved a funding mechanism that allows TEP to recover operating costs, depreciation, property taxes, and a return on investments in company-owned solar projects through RES funds until such costs are reflected in TEP s Base Rates.

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In 2011, the ACC approved TEP s RES implementation plan including investments of $28 million in 2012 and $8 million in 2013 for company-owned solar projects. In 2012, TEP s solar energy investments totaled $28 million. During 2012, TEP earned approximately $2 million pre-tax on its non-rate base investments in solar projects. In 2012, TEP spent $30 million on its 2012 RES implementation plan and met the 2012 renewable energy target of 3.5% of retail kWh sales.

In January 2013, the ACC approved TEP s 2013 RES implementation plan. Under the plan, TEP expects to collect approximately $36 million from retail customers during 2013. The plan includes an investment of $28 million in 2013 for company-owned solar projects, of which $8 million was previously approved by the ACC, as well as the continuation of the funding mechanism for company-owned solar projects. In accordance with the funding mechanism approved by the ACC, TEP could earn approximately $4 million pre-tax in 2013 on solar investments made in 2010, 2011, and 2012. TEP expects to meet the 2013 renewable energy target of 4.0% of retail kWh sales.

Electric Energy Efficiency Standards and Decoupling

In August 2010, the ACC approved new Electric Energy Efficiency Standards (Electric EE Standards) designed to require TEP, UNS Electric, and other affected electric utilities to implement cost-effective programs to reduce customers energy consumption. In 2012, the Electric EE Standards target total kWh savings of 3% of 2011 retail kWh sales; in 2013, the Electric EE Standards target total kWh savings of 5% of 2012 retail kWh sales. The Electric EE Standards increase annually thereafter up to a targeted cumulative annual reduction in retail kWh sales of 22% by 2020. The cumulative annual energy savings from TEP s energy efficiency and DSM programs equaled approximately 2.5% of its 2011 retail kWh sales.

New and existing DSM programs, direct load control programs, and energy efficient building codes are acceptable means to meet the Electric EE Standards as set forth by the ACC. The Electric EE Standards provide for the recovery of costs incurred to implement DSM programs. TEP s programs, and the rates charged to customers for such programs, are subject to annual review and approval by the ACC.

A proposed settlement agreement in TEP s pending rate case proceeding includes a new mechanism for recovery of costs incurred to implement DSM programs. See *Item. 7 Management s Discussion and Analysis of Financial Condition and Result of Operations, Tucson Electric Power, Factors Affecting Results of Operations, 2012 TEP Rate Case, Energy Efficiency Resource Plan.*

Decoupling

In 2010, the ACC issued a policy statement recognizing the need to adopt rate decoupling or another mechanism to make Arizona s Electric EE Standards viable. A decoupling mechanism is designed to encourage energy conservation by restructuring utility rates to separate the recovery of fixed costs from the level of energy consumed. The policy statement allows affected utilities to file rate decoupling proposals in their next general rate case. A proposed settlement agreement in TEP s pending rate case proceeding includes a partial decoupling mechanism. See *Item. 7 Management s Discussion and Analysis of Financial Condition and Result of Operations, Tucson Electric Power, Factors Affecting Results of Operations, 2012 TEP Rate Case, Lost Fixed Cost Recovery Mechanism.*

Retail Electric Competition Rules

In 1999, the ACC approved the Rules that provided a framework for the introduction of retail electric competition in Arizona. Certain portions of the ACC Rules that enabled Electric Service Providers (ESPs) to compete in the retail market were invalidated by an Arizona Court of Appeals decision in 2004. In 2008, the ACC opened an administrative proceeding to address the Rules but has since taken no action. During 2012, a small number of companies filed applications for a Certificate of Convenience and Necessity (CC&N) with the ACC to provide competitive retail electric services in TEP s service territory as an ESP. Unless and until the ACC clarifies the Rules and/or grants a CC&N to an ESP, it is not possible for TEP s retail customers to use an alternative ESP. We cannot predict what changes, if any, the ACC will make to the Rules or if the ACC will grant a CC&N to an ESP.

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TEP S UTILITY OPERATING STATISTICS

	2012	2011	2010	2009	2008
Generation and Purchased Power kWh (000)					
Remote Generation	10,284,612	10,005,127	9,077,032	9,134,183	10,438,864
Local Tucson Generation (Oil, Gas, & Coal)	803,146	906,496	1,492,885	1,131,399	1,016,254
Renewable Generation	44,930	28,049	24,511	23,712	33,776
Purchased Power	2,328,420	2,686,918	2,846,005	3,809,890	3,358,577
Total Generation and Purchased Power	13,461,108	13,626,590	13,440,443	14,099,184	14,847,471
Less Losses and Company Use	789,613	822,220	879,423	936,206	953,036
Total Energy Sold	12,671,495	12,804,370	12,561,010	13,162,978	13,894,435
Sales kWh (000)					
Residential	3,820,637	3,888,011	3,869,540	3,905,696	3,852,707
Commercial	1,973,931	1,972,526	1,963,469	1,988,356	2,034,453
Industrial	2,132,214	2,145,163	2,138,749	2,160,946	2,263,706
Mining	1,092,518	1,083,071	1,079,327	1,064,830	1,095,962
Public Authorities	245,519	243,336	240,703	250,915	255,817
Total Electric Retail Sales	9,264,819	9,332,107	9,291,788	9,370,743	9,502,645
Electric Wholesale Sales	3,406,676	3,472,263	3,269,222	3,792,235	4,391,790
Total Electric Sales	12,671,495	12,804,370	12,561,010	13,162,978	13,894,435
Operating Revenues (000)					
Residential	$ 387,840	$ 383,908	$ 372,212	$ 377,761	$ 351,079
Commercial	228,940	223,621	217,032	219,694	211,639
Industrial	166,739	164,024	159,937	163,720	164,849
Mining	66,158	65,720	62,112	61,033	55,619
Public Authorities	20,910	20,024	19,128	19,865	19,146
RES and DSM	45,292	46,633	37,767	25,443	2,781
Other					415
Total Electric Retail Sales	915,879	903,930	868,188	867,516	805,528
CTC To Be Refunded					(58,092)
Wholesale Revenue- Long-Term	24,910	41,056	55,653	48,249	57,493
Wholesale Revenue- Short-Term	71,257	72,798	71,435	84,410	197,754
California Power Exchange Provision for Wholesale Refunds			(2,970)	(4,172)	
Transmission	15,793	16,392	20,863	18,974	17,173
Other Revenues	133,821	122,210	112,098	84,361	72,292
Total Operating Revenues	$ 1,161,660	$ 1,156,386	$ 1,125,267	$ 1,099,338	$ 1,092,148
Customers (End of Period)					
Residential	369,480	367,396	366,217	365,157	363,861
Commercial	36,214	36,203	35,877	35,759	35,432
Industrial	632	636	635	629	633
Mining	2	2	2	2	2
Public Authorities	62	62	62	61	61
Total Retail Customers	406,390	404,299	402,793	401,608	399,989

Average Retail Revenue per kWh Sold (cents)					
Residential	10.2	9.9	9.6	9.7	9.1
Commercial	11.6	11.3	11.1	11.0	10.4
Industrial and Mining	7.2	7.1	6.9	7.0	6.6
Average Retail Revenue per kWh Sold (excludes RES and DSM)	9.4	9.2	8.9	9.0	8.4
Average Revenue per Residential Customer	$ 1,050	$ 1,045	$ 1,016	$ 1,035	$