

PNM RESOURCES INC
Form 10-K
February 27, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended December 31, 2014

| Commission File Number | Names of Registrants, State of Incorporation, Address and Telephone Number | I.R.S. Employer Identification No. |
|---------------------------|--|---------------------------------------|
| 001-32462 | PNM Resources, Inc. (A New Mexico Corporation) 414 Silver Ave. SW Albuquerque, New Mexico 87102-3289 (505) 241-2700 | 85-0468296 |
| 001-06986 | Public Service Company of New Mexico (A New Mexico Corporation) 414 Silver Ave. SW Albuquerque, New Mexico 87102-3289 (505) 241-2700 | 85-0019030 |
| 002-97230 | Texas-New Mexico Power Company (A Texas Corporation) 577 N. Garden Ridge Blvd. Lewisville, Texas 75067 (972) 420-4189 | 75-0204070 |

Securities Registered Pursuant To Section 12(b) Of The Act:

| Registrant | Title of Each Class | Name of Each Exchange on Which Registered |
|---------------------|-------------------------------|--|
| PNM Resources, Inc. | Common Stock, no par value | New York Stock Exchange |

Securities Registered Pursuant To Section 12(g) Of The Act:

| Registrant | Title of Each Class |
|--------------------------------------|--|
| Public Service Company of New Mexico | 1965 Series, 4.58% Cumulative Preferred Stock (\$100 stated value without sinking fund) |

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

| | | |
|--|------------------------------|-----------------------------|
| PNM Resources, Inc. ("PNMR") | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| Public Service Company of New Mexico ("PNM") | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| Texas-New Mexico Power Company ("TNMP") | YES <input type="checkbox"/> | NO <input type="checkbox"/> |

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

| | | |
|------|------------------------------|-----------------------------|
| PNMR | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| PNM | YES <input type="checkbox"/> | NO <input type="checkbox"/> |

TNMP

YES ü

NO

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

| | | |
|------|------------------------------|-----------------------------|
| PNMR | YES <input type="checkbox"/> | NO |
| PNM | YES <input type="checkbox"/> | NO |
| TNMP | YES | NO <input type="checkbox"/> |

(NOTE: As a voluntary filer, not subject to the filing requirements, TNMP filed all reports under Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months.)

Indicate by check mark whether each 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).

| | | |
|------|------------------------------|----|
| PNMR | YES <input type="checkbox"/> | NO |
| PNM | YES <input type="checkbox"/> | NO |
| TNMP | YES <input type="checkbox"/> | 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 registrants' 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.

Indicate by check mark whether registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Act).

| | Large accelerated filer | Accelerated filer | Non-accelerated filer | Smaller Reporting Company |
|------|----------------------------|----------------------|--------------------------|------------------------------|
| PNMR | <input type="checkbox"/> | | — | |
| PNM | — | | <input type="checkbox"/> | |
| TNMP | — | | <input type="checkbox"/> | |

Indicate by check mark whether the registrants are a shell company (as defined in Rule 12b-2 of the Exchange Act).
YES NO

As of February 20, 2015, shares of common stock outstanding were:

| | |
|------|------------|
| PNMR | 79,653,624 |
| PNM | 39,117,799 |
| TNMP | 6,358 |

On June 30, 2014, the aggregate market value of the voting common stock held by non-affiliates of PNMR as computed by reference to the New York Stock Exchange composite transaction closing price of \$29.33 per share reported by The Wall Street Journal, was \$2,336,240,792. PNM and TNMP have no common stock held by non-affiliates.

PNM AND TNMP MEET THE CONDITIONS SET FORTH IN GENERAL INSTRUCTIONS (I) (1) (a) AND (b) OF FORM 10-K AND ARE THEREFORE FILING THIS FORM WITH THE REDUCED DISCLOSURE FORMAT PURSUANT TO GENERAL INSTRUCTION (I) (2).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following document are incorporated by reference into Part III of this report:

Proxy Statement to be filed by PNMR with the SEC pursuant to Regulation 14A relating to the annual meeting of stockholders of PNMR to be held on May 12, 2015.

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This combined Form 10-K is separately filed by PNMR, PNM, and TNMP. Information contained herein relating to any individual registrant is filed by such registrant on its own behalf. Each registrant makes no representation as to information relating to the other registrants. When this Form 10-K is incorporated by reference into any filing with the SEC made by PNMR, PNM, or TNMP, as a registrant, the portions of this Form 10-K that relate to each other registrant are not incorporated by reference therein.

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GLOSSARY

Definitions:

| | |
|-----------------|---|
| ABO | Accumulated Benefit Obligation |
| Afton | Afton Generating Station |
| AFUDC | Allowance for Funds Used During Construction |
| ALJ | Administrative Law Judge |
| AMS | Advanced Meter System |
| AOCI | Accumulated Other Comprehensive Income |
| APBO | Accumulated Postretirement Benefit Obligation |
| APS | Arizona Public Service Company, the operator and a co-owner of PVNGS and Four Corners |
| ARO | Asset Retirement Obligation |
| ASU | Accounting Standards Update |
| BACT | Best Available Control Technology |
| BART | Best Available Retrofit Technology |
| BDT | Balanced Draft Technology |
| BHP | BHP Billiton, Ltd, the parent of SJCC |
| Board | Board of Directors of PNMR |
| BTU | British Thermal Unit |
| CAA | Clean Air Act |
| CCB | Coal Combustion Byproducts |
| CCN | Certificate of Convenience and Necessity |
| CO ₂ | Carbon Dioxide |
| CTC | Competition Transition Charge |
| D.C. Circuit | United States Court of Appeals for the District of Columbia Circuit |
| Delta | Delta-Person Generating Station |
| DOE | United States Department of Energy |
| DOI | United States Department of Interior |
| EGU | Electric Generating Unit |
| EIB | New Mexico Environmental Improvement Board |
| EIP | Eastern Interconnection Project |
| EIS | Environmental Impact Study |
| EPA | United States Environmental Protection Agency |
| EPE | El Paso Electric |
| ERCOT | Electric Reliability Council of Texas |
| ESA | Endangered Species Act |
| Exchange Act | Securities Exchange Act of 1934 |
| FASB | Financial Accounting Standards Board |
| FERC | Federal Energy Regulatory Commission |
| FIP | Federal Implementation Plan |
| First Choice | FCP Enterprises, Inc. and Subsidiaries |
| Four Corners | Four Corners Power Plant |
| FPL | FPL Energy New Mexico Wind, LLC |
| FPPAC | Fuel and Purchased Power Adjustment Clause |
| GAAP | Generally Accepted Accounting Principles in the United States of America |
| Gallup | City of Gallup, New Mexico |
| GHG | Greenhouse Gas Emissions |
| GWh | Gigawatt hours |

IBEW
IRP
IRS

International Brotherhood of Electrical Workers
Integrated Resource Plan
Internal Revenue Service

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| | |
|--------------------------------|--|
| ISFSI | Independent Spent Fuel Storage Installation |
| KW | Kilowatt |
| KWh | Kilowatt Hour |
| LIBOR | London Interbank Offered Rate |
| Lightning Dock Geothermal | Lightning Dock geothermal power facility, also known as the Dale Burgett Geothermal Plant |
| Lordsburg | Lordsburg Generating Station |
| Luna | Luna Energy Facility |
| MD&A | Management’s Discussion and Analysis of Financial Condition and Results of Operations |
| MMBTU | Million BTUs |
| Moody’s | Moody’s Investor Services, Inc. |
| MW | Megawatt |
| MWh | Megawatt Hour |
| NAAQS | National Ambient Air Quality Standards |
| Navajo Acts | Navajo Nation Air Pollution Prevention and Control Act, Navajo Nation Safe Drinking Water Act, and Navajo Nation Pesticide Act |
| NDT | Nuclear Decommissioning Trusts for PVNGS |
| NEC | Navopache Electric Cooperative, Inc. |
| NEPA | National Environmental Policy Act |
| NERC | North American Electric Reliability Council |
| New Mexico Wind | New Mexico Wind Energy Center |
| Ninth Circuit | United States Court of Appeals for the Ninth Circuit |
| NMAG | New Mexico Attorney General |
| NMED | New Mexico Environment Department |
| NMIEC | New Mexico Industrial Energy Consumers Inc. |
| NMPRC | New Mexico Public Regulation Commission |
| NOx | Nitrogen Oxides |
| NOPR | Notice of Proposed Rulemaking |
| NRC | United States Nuclear Regulatory Commission |
| NSPS | New Source Performance Standards |
| NSR | New Source Review |
| OCI | Other Comprehensive Income |
| OPEB | Other Post Employment Benefits |
| Optim Energy | Optim Energy, LLC, a limited liability company, formerly known as EnergyCo, LLC |
| OSM | United States Office of Surface Mining Reclamation and Enforcement |
| PBO | Projected Benefit Obligation |
| PCRBs | Pollution Control Revenue Bonds |
| PG&E | Pacific Gas and Electric Co. |
| PNM | Public Service Company of New Mexico and Subsidiaries |
| PNM 2013 Term Loan Agreement | PNM’s \$75.0 Million Unsecured Term Loan |
| PNM 2014 Term Loan Agreement | PNM’s \$175.0 Million Unsecured Term Loan |
| PNM Multi-draw Term Loan | PNM’s \$125.0 Million Unsecured Multi-draw Term Loan Facility |
| PNM New Mexico Credit Facility | PNM’s \$50.0 Million Unsecured Revolving Credit Facility |
| | PNM’s \$400.0 Million Unsecured Revolving Credit Facility |

PNM Revolving
Credit Facility

PNMR

PNMR Development

PNM Resources, Inc. and Subsidiaries

PNMR Development and Management Company, an unregulated wholly-owned subsidiary of
PNMR

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| PNMR Term Loan Agreement | PNMR’s \$100.0 Million Unsecured Term Loan |
| PPA | Power Purchase Agreement |
| PSD | Prevention of Significant Deterioration |
| PUCT | Public Utility Commission of Texas |
| PV | Photovoltaic |
| PVNGS | Palo Verde Nuclear Generating Station |
| RCRA | Resource Conservation and Recovery Act |
| RCT | Reasonable Cost Threshold |
| REA | New Mexico’s Renewable Energy Act of 2004 |
| REC | Renewable Energy Certificates |
| Red Mesa Wind | Red Mesa Wind Energy Center |
| REP | Retail Electricity Provider |
| Rio Bravo | Rio Bravo Generating Station, formerly know as Delta |
| RMC | Risk Management Committee |
| ROE | Return on Equity |
| RPS | Renewable Energy Portfolio Standard |
| RSIP | Revised State Implementation Plan |
| SCE | Southern California Edison Company |
| SCPPA | Southern California Public Power Authority |
| SCR | Selective Catalytic Reduction |
| SEC | United States Securities and Exchange Commission |
| SIP | State Implementation Plan |
| SJCC | San Juan Coal Company |
| SJGS | San Juan Generating Station |
| SJPPA | San Juan Project Participation Agreement |
| SNCR | Selective Non-Catalytic Reduction |
| SO ₂ | Sulfur Dioxide |
| SPS | Southwestern Public Service Company |
| SRP | Salt River Project |
| S&P | Standard and Poor’s Ratings Services |
| TCEQ | Texas Commission on Environmental Quality |
| TECA | Texas Electric Choice Act |
| Tenth Circuit | United States Court of Appeals for the Tenth Circuit |
| TNMP | Texas-New Mexico Power Company and Subsidiaries |
| TNMP 2011 Term Loan Agreement | TNMP’s \$50.0 Million Secured Term Loan |
| TNMP Revolving Credit Facility | TNMP’s \$75.0 Million Secured Revolving Credit Facility |
| TNP | TNP Enterprises, Inc. and Subsidiaries |
| Tri-State | Tri-State Generation and Transmission Association, Inc. |
| Tucson | Tucson Electric Power Company |
| UAMPS | Utah Associated Municipal Power System |
| Valencia | Valencia Energy Facility |
| VaR | Value at Risk |
| WACC | Weighted Average Cost of Capital |

WEG
WSP

WildEarth Guardians
Western Systems Power Pool

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PART I

ITEM 1. BUSINESS

THE COMPANY

Overview

PNMR is an investor-owned holding company with two regulated utilities providing electricity and electric services in New Mexico and Texas. PNMR's electric utilities are PNM and TNMP. PNMR is focused on achieving the following strategic goals:

- Earning authorized returns on its regulated businesses
- Continuing to improve credit ratings
- Providing a top quartile total return to investors

PNMR's success in accomplishing these strategic goals is highly dependent on continued favorable regulatory treatment for its regulated utilities. Both PNM and TNMP seek cost recovery for their investments through general rate cases and various rate riders. PNM filed a general rate case with the NMPRC in December 2014. Additional information about rate filings is provided in Operations and Regulation below and in Note 17.

PNMR's common stock trades on the New York Stock Exchange under the symbol PNM. PNMR was incorporated in the State of New Mexico in 2000.

Other Information

These filings for PNMR, PNM, and TNMP include disclosures for each entity. For discussion purposes, this report uses the term "Company" when discussing matters of common applicability to PNMR, PNM, and TNMP. Discussions regarding only PNMR, PNM, or TNMP are so indicated. A reference to "MD&A" in this report refers to Part II, Item 7. –Management's Discussion and Analysis of Financial Condition and Results of Operations. A reference to a "Note" refers to the accompanying Notes to Consolidated Financial Statements.

Financial information relating to amounts of revenue, net income, and total assets of reportable segments is contained in MD&A and Note 2.

WEBSITES

The PNMR website, www.pnmresources.com, is an important source of Company information. New or updated information for public access is routinely posted. PNMR encourages analysts, investors, and other interested parties to register on the website to automatically receive Company information by e-mail. This information includes news releases, notices of webcasts, and filings with the SEC. Participants can unsubscribe at any time and will not receive information that was not requested.

Our corporate Internet addresses are:

• PNMR: www.pnmresources.com

• PNM: www.pnm.com

• TNMP: www.tnmp.com

In addition to the corporate websites, PNM established a website, www.PowerforProgress.com, dedicated to showing how it balances delivering reliable power at affordable prices and protecting the environment. This website is designed to be a resource for the facts about PNM's operations and support efforts, including plans for building a

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sustainable energy future for New Mexico. The contents of these websites are not a part of this Form 10-K. The SEC filings of PNMR, PNM, and TNMP, including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, are accessible free of charge on the PNMR website as soon as reasonably practicable after they are filed with, or furnished to, the SEC. These reports are also available in print upon request from PNMR free of charge.

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Also available on the Company's website at <http://www.pnmresources.com/corporate-governance.aspx> and in print upon request from any shareholder are our:

Corporate Governance Principles

- Code of Ethics (Do the Right Thing – Principles of Business Conduct)

• Charters of the Audit and Ethics Committee, Nominating and Governance Committee, Compensation and Human Resources Committee, and Finance Committee

The Company will post amendments to or waivers from its code of ethics (to the extent applicable to the Company's executive officers and directors) on its website.

OPERATIONS AND REGULATION

Regulated Operations

PNM

PNM is an electric utility that provides electric generation, transmission, and distribution service to its rate-regulated customers. In New Mexico, the utility's retail electric service territory covers a large area of north central New Mexico, including the cities of Albuquerque, Rio Rancho, and Santa Fe, and certain areas of southern New Mexico. PNM also provides electricity to firm-requirements wholesale customers in New Mexico and Arizona. Service to retail electric customers is subject to the jurisdiction of the NMPRC. Service to wholesale customers is regulated by FERC. Regulation encompasses the utility's electric rates, service, accounting, issuances of securities, construction of major new generation, types of generation resources, transmission and distribution facilities, and other matters.

Other services provided by PNM include transmission services to third parties as well as the generation and sale of electricity into the wholesale market, which services are regulated by FERC. PNM owns or leases transmission lines, interconnected with other utilities in New Mexico, Texas, Arizona, Colorado, and Utah. The largest retail electric customer served by PNM accounted for 3.4% of the utility's revenues for the year ended December 31, 2014. PNM was incorporated in the State of New Mexico in 1917.

NMPRC Regulated Retail Rate Proceedings

Customer rates for retail electric service are set by the NMPRC. PNM filed a general rate case with the NMPRC in December 2014. PNM's application proposes a revenue increase of \$107.4 million, effective January 1, 2016, based on a calendar 2016 future year test and a ROE of 10.5%. PNM requested this increase to account for infrastructure investments made since its last rate case and investments needed in the next two years to provide reliable service to PNM's retail customers, as well as to reflect declining sales growth in PNM's service territory. PNM is proposing several changes to rate design to establish fair and equitable pricing across rate classes and to better align cost recovery with cost causation, including an access charge to customers installing photovoltaic systems after December 31, 2015. See Note 17 for additional information concerning this filing.

PNM's previous general rate case filing was made in June 2010. In August 2011, the NMPRC issued a final order that included, among other things, a \$72.1 million increase in annual non-fuel revenues for New Mexico retail customers. As permitted by that order, PNM filed an application in January 2012 for a rate rider to collect costs for renewable energy procurements incurred after December 31, 2010 that are not otherwise being collected in rates. The rider will terminate upon a final order in PNM's next general rate case unless that order authorizes a continuation of the rider. As a separate component of the rider, if PNM's earned return on jurisdictional equity in a calendar year, adjusted for weather and other items not representative of normal operation, exceeded 10.5%, it would refund to customers during

May through December of the following year the amount over 10.5%. PNM's earned return on jurisdictional equity did not exceed 10.5% in 2013 or 2014.

FERC Regulated Wholesale Operations

In October 2010, PNM filed a notice with FERC to increase its wholesale electric transmission rates for all of PNM's wholesale electric transmission service customers, which include other utilities, electric cooperatives, and entities that use PNM's transmission system to transmit power at the wholesale level. The proposed rates were implemented on June 1, 2011, subject to refund. On January 2, 2013, FERC approved a settlement among the parties providing for an increase in transmission service revenues of \$2.9 million annually.

In December 2012, PNM filed a notice with FERC to increase its wholesale electric transmission rates for all of its transmission customers. The filing represents a formula based rate as contemplated by the approved settlement in the case described

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above. The proposed increase of \$1.3 million, as updated, went into effect, subject to refund, on August 2, 2013. On May 1, 2014, PNM updated its formula rate incorporating 2013 data resulting in a \$0.5 million rate increase over the then current rates. The updated rate request went into effect on May 30, 2014, subject to refund. The parties have engaged in settlement negotiations and PNM anticipates that a settlement will be filed with FERC in the near future. There is no required time frame for FERC to act upon a settlement. PNM is unable to predict the outcome of this proceeding.

PNM has entered into firm-requirements wholesale contracts to provide electricity to various customers. These contracts contain both capacity charges and energy charges. Capacity charges are monthly payments for a commitment of resources to service the contract requirements. Energy charges are payments based on the amount of electricity delivered to the customer and are intended to compensate for the variable costs incurred to provide the energy. The average billing demands for PNM's firm-requirements wholesale customers aggregate approximately 62 MW, excluding the contract with Gallup that expired in 2014. No firm-requirements customer of PNM accounted for more than 2.5% of PNM's revenues for the year ended December 31, 2014.

In September 2011, PNM filed with FERC to increase rates for electric service and ancillary services provided to NEC, PNM's largest firm-requirements wholesale customer. PNM also requested a traditional FPPAC and full recovery of certain third-party transmission charges. FERC issued an order allowing the increased rates to be collected beginning April 14, 2012, subject to refund. The parties agreed to a settlement providing for an increase in rates of \$5.3 million and an extension of the contract for 10 years through December 31, 2035. FERC approved the settlement in April 2013. PNM provided both energy and power services to Gallup, which was its second largest firm-requirements wholesale customer, under an electric service agreement that expired on June 30, 2014. PNM's recently filed general rate case discussed above includes a reallocation of costs among regulatory jurisdictions reflecting the termination of the contract to serve Gallup. See Results of Operations in MD&A and Note 17.

PNM also provides electricity at wholesale to the City of Aztec, New Mexico under a contract that expires on June 30, 2016. In 2014, PNM entered into a contract with the Jicarilla Apache Nation to provide electricity at wholesale through May 8, 2016, which date can be extended through May 8, 2019, if approved by the NMPRC.

PNM's current authorization under FERC regulation requires that revenue requirements for sales of electricity at wholesale are to be based on PNM's costs of providing such service. In August 2014, PNM filed an application with FERC to allow PNM to enter into arrangements to sell electricity at wholesale prices within PNM's balancing authority area using rates that are based on market conditions. There is no statutory requirement for FERC to act upon this application within a specified period of time. PNM cannot predict if FERC will grant the request to sell at market-based rates.

Operational Information

Weather-normalized retail electric KWh sales decreased by 1.7% in 2014 and 1.8% in 2013. The system peak demands for retail and firm-requirements customers decreased in 2014 and increased in 2013. The system peak demands were as follows:

System Peak Demands

| | 2014 (Megawatts) | 2013 | 2012 |
|--------|---------------------|-------|-------|
| Summer | 1,878 | 2,008 | 1,948 |
| Winter | 1,471 | 1,576 | 1,523 |

PNM holds long-term, non-exclusive franchise agreements for its electric retail operations, with varying expiration dates. These franchise agreements allow the utility to access public rights-of-way for placement of its electric facilities. Franchise agreements have expired in some areas PNM serves, including Albuquerque, Rio Rancho, and Santa Fe. Because PNM remains obligated under New Mexico state law to provide service to customers in these areas, the expirations should not have a material adverse impact. The Albuquerque, Rio Rancho, and Santa Fe metropolitan areas accounted for 48.0%, 10.5%, and 9.6% of PNM's 2014 revenues and no other franchise area represents more than 5%. Although PNM is not required to collect or pay franchise fees in some areas it serves, the utility continues to collect and pay such fees in certain parts of its service territory, including Albuquerque, Rio Rancho, and Santa Fe.

As discussed in Note 16, the County Commission of Bernalillo County, New Mexico passed an ordinance on January 28, 2014 that would require PNM and other utilities to enter into a use agreement and pay a yet to be determined fee as a condition for installing, maintaining, and operating facilities on county rights-of-way. PNM and other utilities have filed complaints in federal and state courts challenging the validity of the ordinance. If the challenge to the ordinance is unsuccessful, PNM believes

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any fees paid pursuant to the ordinance would be considered franchise fees and would be recoverable from customers. PNM is unable to predict the outcome of this matter.

PNM owns or leases 3,197 circuit miles of electric transmission lines that interconnect with other utilities in New Mexico, Arizona, Colorado, Texas, and Utah. There has been little development of new transmission facilities in recent years. Therefore, most of the capacity on PNM's transmission system is fully committed during peak hours, with very little to no additional access available on a firm commitment basis. These factors result in physical constraints on the system and limit the ability to wheel power into PNM's service area from outside of New Mexico.

PNM also generates and sells electricity into the wholesale market. Because PNM's 134 MW share of Unit 3 at PVNGS currently is excluded from retail rates, that unit's power is being sold in the wholesale market and any earnings or losses are realized by shareholders. PNM has contracted to sell 100% of PVNGS Unit 3 output through 2015, at market price plus a premium. Through hedging arrangements that are accounted for as economic hedges, PNM has established fixed rates for substantially all of these sales. As discussed in Note 16, PNM has requested NMPRC approval to include PVNGS Unit 3 as a jurisdictional resource to serve New Mexico retail customers beginning in 2018 as part of the revised plan to comply with the regional haze requirements of the CAA. Beyond the PVNGS contracts, PNM also engages in activities to optimize its existing jurisdictional assets and long-term power agreements through spot market, hour ahead, day ahead, week ahead, and other sales of any excess generation not required to fulfill retail load and contractual commitments. Ninety percent of the margins from these optimization sales are credited to retail customers through the FPPAC.

Use of Future Test Year

Under New Mexico law, the NMPRC must set rates using the test period, including a future test year, that best reflects the conditions the utility will experience when new rates are anticipated to go into effect. In addition, the NMPRC must include certain construction work in progress ("CWIP") for environmental improvement, generation, and transmission projects in rate base. These provisions are designed to promote more timely recovery of reasonable costs of providing utility service.

The use of a future test year should help PNM mitigate the adverse effects of regulatory lag, which is inherent when using a historical test year. Accordingly, the utility's earnings should more closely reflect the rate of return allowed by the NMPRC. PNM believes that achieving earnings that approximate its allowed rate of return is an important factor in attracting equity investors, as well as being considered favorably by credit rating agencies and financial analysts.

As discussed above, in December 2014, PNM filed a request for a general rate increase with the NMPRC, which is based on a 2016 future test year. As with any forward looking financial information, utilizing a future test year in a rate filing presents challenges that exist in the forecasting process. These include forecasts of both operating and capital expenditures that necessitate reliance on many assumptions concerning future conditions and operating results. In the rate making process, PNM's assumptions are subject to challenge by regulators and intervenors who may assert different interpretations or assumptions.

Renewable Portfolio Standard

The REA was enacted to encourage the development of renewable energy in New Mexico. The act establishes a mandatory RPS requiring a utility to acquire a renewable energy portfolio equal to 10% by 2011, 15% by 2015, and 20% by 2020. The act provides for streamlined proceedings for approval of utilities' renewable energy procurement plans, assures utilities recovery of costs incurred consistent with approved procurement plans, and requires the NMPRC to establish a RCT for the procurement of renewable resources to prevent excessive costs being added to

rates. PNM files required renewable energy plans with the NMPRC annually and makes procurements consistent with the plans approved by the NMPRC. See Note 17.

TNMP

TNMP is a regulated utility operating in Texas. TNMP's predecessor was organized in 1925. TNMP is incorporated in the State of Texas.

TNMP provides transmission and distribution services in Texas under the provisions of TECA and the Texas Public Utility Regulatory Act. TNMP is subject to traditional cost-of-service regulation with respect to rates and service under the jurisdiction of the PUCT and certain municipalities. Because its transmission and distribution activities are solely within ERCOT, TNMP is not subject to traditional rate regulation by FERC. TNMP serves a market of small to medium sized communities, most of which have populations of less than 50,000. TNMP is the exclusive provider of transmission and distribution services in most areas it serves.

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TNMP's service territory consists of three non-contiguous areas. One portion of this territory extends from Lewisville, which is approximately 10 miles north of the Dallas-Fort Worth International Airport, eastward to municipalities near the Red River, and to communities north, west, and south of Fort Worth. The second portion of its service territory includes the area along the Texas Gulf Coast between Houston and Galveston, and the third portion includes areas of far west Texas between Midland and El Paso. ERCOT is the independent system operator that is responsible for maintaining reliable operations for the bulk electric power supply system in its region.

TNMP provides transmission and distribution services at regulated rates to various REPs that, in turn, provide retail electric service to consumers within TNMP's service area. TNMP experienced increases in weather-normalized retail KWh sales of 3.2% in 2014 and 2.6% in 2013. As of December 31, 2014, 94 active REPs receive transmission and distribution services from TNMP. The acquirer of First Choice, including the former First Choice operations, accounted for 15% of TNMP's revenues in 2014. Two other unaffiliated customers of TNMP accounted for operating revenues of 15% and 11% in 2014. No other customer accounted for more than 10% of revenues.

Regulatory Activities

In July 2011, the PUCT approved a settlement and authorized an AMS deployment plan that permits TNMP to collect \$113.4 million in deployment costs through a surcharge over a 12-year period. TNMP began collecting the surcharge on August 11, 2011. Deployment of smart meters began in September 2011 and is scheduled to be completed over a 5-year period.

The PUCT approved interim adjustments to TNMP's transmission rates of \$2.5 million on September 27, 2012, \$2.9 million on March 20, 2013, \$2.8 million on September 17, 2013, \$2.9 million on March 13, 2014, and \$4.2 million on September 8, 2014. On January 16, 2015, TNMP filed an application to further update its transmission rates, which would increase revenues by \$4.4 million annually. The application is pending before the PUCT.

Franchise Agreements

TNMP holds long-term, non-exclusive franchise agreements for its electric transmission and distribution services. These agreements have varying expiration dates and some have expired. TNMP intends to negotiate and execute new or amended franchise agreements with municipalities where the agreements have expired or will be expiring. Since TNMP is the exclusive provider of transmission and distribution services in most areas that it serves, the need to renew or renegotiate franchise agreements should not have a material adverse impact. TNMP also earns revenues from service provided to facilities in its service area that lie outside the territorial jurisdiction of the municipalities with which TNMP has franchise agreements.

Corporate and Other

The Corporate and Other segment includes PNMR holding company activities, primarily related to corporate level debt and PNMR Services Company. PNMR Services Company provides corporate services through shared services agreements to PNMR and all of PNMR's business units, including PNM and TNMP. These services are charged and billed at cost on a monthly basis to the business units.

SOURCES OF POWER

PNM

Generation Capacity

As of December 31, 2014, the total net generation capacity of facilities owned or leased by PNM was 2,397 MW. PNM also obtains power under a long-term PPA for the power produced by New Mexico Wind, which has a capacity of 204 MW, and the output of the Lightning Dock Geothermal facility, which currently has a capacity of 4 MW. On January 1, 2015, PNM began obtaining the power output of Red Mesa Wind, which has a capacity of 102 MW.

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PNM's capacity in electric generating facilities, which are owned, leased, or under PPAs, in commercial service as of January 1, 2015 is:

| Type | Name | Location | Generation Capacity (MW) |
|------|----------------|-----------------------|--------------------------|
| Coal | SJGS | Waterflow, New Mexico | 783 |
| Coal | Four Corners | Fruitland, New Mexico | 200 |
| Gas | Reeves Station | | |