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TUCSON ELECTRIC POWER CO  
Form DEF 14A  
April 07, 2004

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the  
Securities Exchange Act of 1934  
(Amendment No. )

Filed by the Registrant  [X]  
Filed by a Party other than the Registrant  [ ]

Check the appropriate box:

- [ ] Preliminary Proxy Statement  
 [ ] Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))  
 [X] Definitive Proxy Statement  
 [ ] Definitive Additional Materials  
 [ ] Soliciting Material Pursuant to Sections 240.14a-11(c) or 240.14a-12

UNISOURCE ENERGY CORPORATION

-----  
(Name of the Registrant as Specified In Its Charter)  
-----

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- [X] No fee required.  
 [ ] Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.  
1) Title of each class of securities to which transaction applies:  
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3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11(set forth the amount on which the filing fee is calculated and state how it was determined):  
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1) Amount Previously Paid:  
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3) Filing Party:  
4) Date Filed:

UNISOURCE ENERGY  
One South Church Avenue

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Tucson, Arizona 85701

April 7, 2004

James S. Pignatelli  
Chairman of the Board

(520) 571-4000

Dear Shareholders:

On March 29, 2004, at a special meeting of our shareholders, we obtained shareholder approval of the acquisition agreement that provides for an affiliate of Saguaro Utility Group L.P. to acquire all of our outstanding shares of common stock for \$25.25 per share. The completion of the acquisition still requires the approval of several regulatory agencies and the satisfaction of the other closing conditions contained in the acquisition agreement. We expect that the acquisition will be consummated in the second half of 2004.

Until the completion of the acquisition, we will continue to function as a public company. In that regard, it is now appropriate for us to hold the 2004 Annual Shareholders' Meeting for the election of directors. You are cordially invited to attend the 2004 Annual Shareholders' Meeting to be held on Friday, May 7, 2004, at the Marriott University Park Hotel, 880 East Second Street, Tucson, Arizona. The meeting will begin promptly at 10:00 a.m., so please plan to arrive earlier. No admission tickets will be required for attendance at the meeting.

Directors and officers will be available before and after the meeting to speak with you. During the meeting, we will answer your questions regarding our business affairs and we will consider the matters explained in the enclosed Proxy Statement.

We have enclosed a proxy card that lists all matters that require your vote. Please complete, sign, date and mail the proxy card as soon as possible, whether or not you plan to attend the meeting. You may also vote by telephone or the Internet, as explained on the enclosed proxy card. If you attend the meeting and wish to vote your shares personally, you may revoke your proxy at that time. Your interest and continued support of UniSource Energy Corporation are much appreciated.

Sincerely,

UNISOURCE ENERGY CORPORATION

/s/ James S. Pignatelli

-----  
James S. Pignatelli  
Chairman of the Board, President and  
Chief Executive Officer

NOTICE OF ANNUAL SHAREHOLDERS' MEETING

To the Holders of Common Stock of  
UniSource Energy Corporation

We will hold the 2004 Annual Shareholders' Meeting ("Meeting") of

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UniSource Energy Corporation at the Marriott University Park Hotel, 880 East Second Street, Tucson, Arizona, on Friday, May 7, 2004, at 10:00 a.m., Mountain Standard Time. The purpose of the Meeting is to:

1. elect nine directors to our Board of Directors for the ensuing year; and
2. consider any other matters which properly come before the Meeting.

Only shareholders of record at the close of business on March 29, 2004, are entitled to vote at the Meeting.

We have enclosed our 2003 Annual Report, including audited financial statements, and the Proxy Statement with this notice. Proxy soliciting material is first being sent or given to shareholders on or about April 7, 2004. Your proxy is being solicited by our Board of Directors.

Please complete, sign, date and mail the enclosed proxy card as soon as possible, or vote by telephone or the Internet, as explained on the enclosed proxy card.

/s/Catherine A. Nichols

-----  
Catherine A. Nichols  
Corporate Secretary

Dated: April 7, 2004

### YOUR VOTE IS IMPORTANT

EACH SHAREHOLDER IS URGED TO COMPLETE, SIGN, DATE AND RETURN PROMPTLY THE ENCLOSED PROXY CARD BY MAIL, OR TO VOTE BY TELEPHONE OR THE INTERNET, AS EXPLAINED ON THE ENCLOSED PROXY CARD. IF THE MAIL OPTION IS SELECTED, USE THE ENCLOSED ENVELOPE, WHICH DOES NOT REQUIRE POSTAGE IF MAILED IN THE UNITED STATES. RETURNING A SIGNED PROXY WILL NOT PROHIBIT YOU FROM ATTENDING THE MEETING AND VOTING IN PERSON IF YOU SO DESIRE.

### UNISOURCE ENERGY CORPORATION

One South Church Avenue  
Tucson, Arizona 85701

### ANNUAL SHAREHOLDERS' MEETING PROXY STATEMENT

Annual Meeting	May 7, 2004 10:00 a.m., MST	Marriott University Park Hotel 880 East Second Street Tucson, Arizona 85719
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Record Date	The record date is March 29, 2004 ("Record Date"). If you were a shareholder of record at the close of business on the Record Date, you may vote at the 2004 Annual Shareholders' Meeting ("Meeting") of UniSource Energy Corporation ("UniSource Energy" as well as
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references to "we," "our" and "us"). At the close of business on the Record Date, we had 34,037,640 shares of common stock outstanding.

Agenda	1. Proposal One: Elect nine directors to our Board of Directors ("Board") for the ensuing year.  2. Consider any other matters which properly come before the Meeting and any adjournments.
Independent Auditors	Representatives of PricewaterhouseCoopers, LLP are expected to be present at the Meeting with the opportunity to make a statement and respond to appropriate questions from our shareholders.
Proxies	A form of proxy for execution by shareholders is enclosed. Unless you tell us on the proxy card to vote differently, we will vote signed returned proxies "for" the Board's nominees. The Board or proxy holders will use their discretion on other matters that properly come before the Meeting. If a nominee cannot or will not serve as a director, the Board or the persons designated as proxies will vote for a person whom they believe will carry on our present policies.
We will follow your voting instructions. If none, we will vote signed proxies "for" the nominees.	
Proxies Solicited By	The Board.
First Mailing Date	We anticipate first mailing this Proxy Statement along with the proxy on or about April 7, 2004.
Revoking Your Proxy	You may revoke your proxy before it is voted at the Meeting. To revoke, follow the procedures listed on page 2 under "Voting Procedures/Revoking Your Proxy."
Comments	Your comments about any aspects of our business are welcome. You may use the space provided on the proxy card for this purpose, if desired. Although we may not respond on an individual basis, your comments help us to measure your satisfaction, and we may benefit from your suggestions.
We welcome your comments. The proxy card has room for them.	

PLEASE VOTE - YOUR VOTE IS IMPORTANT  
Prompt return of your proxy will help reduce the costs of re-solicitation.

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VOTING PROCEDURES/REVOKING YOUR PROXY

You can vote by  
 by telephone, the  
 Internet, mail or in  
 person. We encourage  
 you to vote by  
 telephone or the  
 Internet to help us  
 save money.

You can vote your shares by telephone, the Internet,  
 mail or in person at the Meeting. Your proxy card  
 contains instructions for voting by telephone or the  
 Internet, which are the least expensive and fastest  
 methods of voting. To vote by mail, complete, sign and  
 date your proxy card, or your broker's voting  
 instruction card if your shares are held by your  
 broker, and return it in the enclosed return envelope.

Under Arizona law, a majority of the shares  
 entitled to vote on any single matter which may be  
 brought before the Meeting will constitute a  
 quorum. Business may be conducted once a quorum is  
 represented at the Meeting. Except as otherwise  
 specified by law or in our Articles of  
 Incorporation or Bylaws, if a quorum exists, action  
 on a matter other than the election of directors  
 will be deemed approved if the votes cast in favor  
 of the matter exceed votes cast against it.

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Directors are elected by a plurality of the votes  
 cast by the shares entitled to vote if a quorum is  
 present. A plurality means receiving the largest  
 number of votes, regardless of whether that is a  
 majority. Withheld votes will be counted as being  
 represented at the Meeting for quorum purposes but  
 will not have an effect on the vote.

You may cumulate your  
 votes for directors.

In the election of directors, each shareholder has  
 the right to cumulate his votes by casting as many  
 votes in the aggregate equal to the number of his  
 shares of common stock multiplied by the number of  
 directors to be elected. He may cast all of such votes  
 for one nominee or distribute such votes among two or  
 more nominees. For any other matter that may properly  
 come before the Meeting, each share of common stock  
 will be entitled to one vote.

You can revoke your

Any shareholder giving a proxy has a right to revoke

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proxy after sending it in by following these procedures.

that proxy by giving notice to UniSource Energy in writing directed to the Corporate Secretary, UniSource Energy Corporation, One South Church Avenue, Suite 1820, Tucson, Arizona 85701, or in person at the Meeting at any time before the proxy is exercised. Those who fail to return a proxy or fail to attend the Meeting will not count towards determining any required plurality, majority or quorum.

The shares represented by an executed proxy will be voted for the election of directors or withheld in accordance with the specifications in the proxy. If no specification is made in an executed proxy, the proxy will be voted in favor of the nominees as set forth herein.

### Proxy Solicitation

We will bear the entire cost of the solicitation of proxies. Solicitations will be made primarily by mail. Additional solicitation of brokers, banks, nominees and institutional investors may be made pursuant to a special engagement of DF King & Co., Inc., at a cost of approximately \$7,500 plus reasonable out-of-pocket expenses. Solicitations may also be made by telephone, facsimile or personal interview, if necessary, to obtain reasonable representation of shareholders at the Meeting. Our employees may solicit proxies for no additional compensation. We will request brokers or other persons holding stock in their names, or in the names of their nominees, to forward proxy materials to the beneficial owners of such stock or request authority for the execution of the proxies. We will reimburse brokers and other persons for reasonable expenses they incur in sending these proxy materials to you if you are a beneficial holder of our shares.

### PROPOSED ACQUISITION OF UNISOURCE ENERGY

On November 21, 2003, we entered into an acquisition agreement with an affiliate of Saguaro Utility Group L.P., an Arizona limited partnership ("Saguaro Utility"). The acquisition agreement provides for the affiliate of Saguaro Utility to acquire all of our outstanding shares of common stock for \$25.25 per share. Saguaro Utility will merge its affiliate with and into us. We will survive the merger as a wholly owned indirect subsidiary of Saguaro Utility. Trading in our common stock on the New York Stock Exchange and the Pacific Stock Exchange will cease immediately as of the effective time of the acquisition. After that time, the surviving corporation will delist our shares from the New York Stock Exchange and the Pacific Stock Exchange and deregister our shares under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Our headquarters will

remain in Tucson, and we expect that our senior

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management team will remain generally in place. We received shareholder approval of the acquisition agreement on March 29, 2004. The completion of the acquisition still requires the approval of several regulatory agencies and the satisfaction of the other closing conditions contained in the acquisition agreement. We expect that the acquisition will be consummated in the second half of 2004. See "Effect of Proposed Acquisition on Compensation" on page 18 of this Proxy Statement.

UNISOURCE ENERGY SHARE OWNERSHIP

Security Ownership of Management The following table sets forth the number and percentage of shares beneficially owned as of the Record Date and the nature of such ownership by each of our directors (all of which are nominees), our Chief Executive Officer and our five other most highly compensated executive officers at December 31, 2003 (the "Named Executives") and all directors and officers as a group. Ownership includes direct and indirect (beneficial) ownership, as defined by the SEC rules.

Title of Class -----	Name and Amount and Title of Beneficial Owner -----	Nature of Beneficial Ownership (1) -----
Common	James S. Pignatelli Chairman, President and Chief Executive Officer	744,282 (2)
Common	Lawrence J. Aldrich Director	9,624 (3)
Common	Larry W. Bickle Director	15,564 (4)
Common	Elizabeth T. Bilby Director	13,625 (5)
Common	Harold W. Burlingame Director	12,225 (4)
Common	John L. Carter Director	22,371 (6)
Common	Robert A. Elliott Director	405
Common	Kenneth Handy Director	6,359 (7)
Common	Warren Y. Jobe Director	4,359 (7)
Common	Steven J. Glaser Senior Vice President and Chief Operating Officer, Transmission	199,679 (8)

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& Distribution - Tucson Electric  
Power Company ("TEP")

Common	Dennis R. Nelson Senior Vice President and Chief Operating Officer - UniSource Energy Services, Inc. ("UES")	198,300 (9)
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Title of Class -----	Name and Amount and Title of Beneficial Owner -----	Nature of Beneficial Ownership (1) -----
Common	Michael J. DeConcini Senior Vice President, Investments and Planning / Senior Vice President and Chief Operating Officer, Energy Resources - TEP	145,023 (10)
Common	Kevin P. Larson Vice President, Chief Financial Officer and Treasurer	126,210 (11)
Common	Vincent Nitido, Jr. Vice President, General Counsel and Chief Administrative Officer	149,303 (12)
Common	All directors and executive officers as a group	2,078,620 (13)

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Security Ownership of Certain Beneficial Owners As of March 29, 2004, based on information reported in filings made by the following persons with the SEC or information otherwise known to us, the following persons were known or reasonably believed to be, as more fully described below, the beneficial owners of more than 5% of our commonstock:

Title of Class -----	Name and Address of Beneficial Owner -----	Amount and Nature of Beneficial Ownersh -----
Common	T. Rowe Price Associates, Inc. 100 E. Pratt Street Baltimore, MD 21202	3,237,005 (1)
Common	Gabelli Asset Management Inc.	2,781,599 (2)



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	One Corporate Center Rye, NY 10580-1435	
Common	White Mountains Insurance Group 80 South Main Street Hanover, NH 03755	1,798,100 (3)
Common	BNP Paribas, SA 16 Boulevard des Italiens 75009 Paris, France	1,796,010 (4)
Common	Barclays Private Bank Limited 59/60 Grosvenor Street London, W1X 9DA England	1,718,794 (5)

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Section 16(a) Beneficial Ownership Reporting Compliance Section 16(a) of the Exchange Act and SEC regulations require directors, certain officers and persons who own greater than 10% of our stock to file reports of ownership and changes in ownership of such stock with the SEC and the New York Stock Exchange. These directors, officers and greater than 10% beneficial owners are required by law to furnish us with copies of all forms they file under Section 16(a).

Based solely on a review of the copies of such forms furnished to us and on written representations of our directors and officers, we believe that all Section 16(a) filing requirements applicable to our directors and officers were complied with during 2003.

PROPOSAL ONE: ELECTION OF DIRECTORS

General At the Meeting, our shareholders of record will elect nine directors to serve on our Board for the ensuing year and until their successors are elected and qualified. The shares represented by executed proxies in the form enclosed, unless withheld, will be voted for the nine nominees listed below, or, in the discretion of the persons acting as proxies, will be voted cumulatively for one or more of such nominees. All of the current nominees are present members of the Board. All of the nominees have consented to serve if elected. If any nominee becomes unavailable for any reason, or a vacancy should occur before the election, it is the intention of the persons designated as proxies to vote, in their discretion, for other nominees.

We will elect nine directors this year.

BOARD NOMINEES

James S. Pignatelli Chairman of the Board, President and Chief Executive Officer of UniSource Energy since July 1998; Senior Vice President and Chief Operating Officer of UniSource Energy from December 1997 to July 1998; Chairman of the Board of Directors, President and Chief Executive Officer of TEP, the principal subsidiary of UniSource Energy, since July 1998; Executive Vice President and Chief Operating Officer

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of TEP from March 1998 to July 1998; Senior Vice President and Chief Operating Officer of TEP from 1996 to 1998; Chairman of the Board of Directors, President and Chief Executive Officer of Millennium Energy Holdings, Inc. ("Millennium"), a wholly owned subsidiary of UniSource Energy, since 1997. Board member since 1998. Age 60.

Lawrence J. Aldrich (4) General Partner, Valley Ventures III, LP, since September 2002; Managing Director and Founder, Tucson Ventures, LLC, from February 2000 to September 2002; President and Chief Executive Officer of Tucson Newspapers from January 1992 to February 2000; Director of TEP and Millennium since 2000. Board member since 2000. Age 51.

Larry W. Bickle (4) Managing Director of Haddington Ventures, LLC, an investment company, since 1997; Director of St. Mary Land and Exploration since 1995; Director of Millennium since 1998. Board member since 1998. Age 58.

Elizabeth T. Bilby (1) (2) (3) President of Gourmet Products, Inc., an agricultural product marketing company; Director of Marketing of Green Valley Pecans since 1982. Director of TEP since 1995; Director of Millennium from 1998-2003. Board member since 1995. Age 64.

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Harold W. Burlingame (1) (3) Senior Executive Advisor for AT&T Wireless Services since July 2001; Executive Vice President, Communications and Human Resources of AT&T Wireless Services from April 2000 to June 2001; Executive Vice President, Merger and Joint Venture Integration of AT&T from March 1999 to March 2000; Executive Vice President of Human Resources of AT&T from 1987 to March 1999; Member of the AT&T Foundation from November 1986 to December 2002; Chair, Executive Committee, Organization Resources Counselors since June 1999; Director of TEP since 1998. Board member since 1998. Age 63.

John L. Carter (1) (2) (3) (4) Retired as General Manager of the Tucson, Arizona office of IBM in 1987. President and Chief Executive Officer of Qualtronic Manufacturing, Inc. from 1987 to 1993. Retired as Executive Vice President and Chief Financial Officer of Burr-Brown Corporation in 1996. Director of TEP since 1996; Director of Millennium since 1998. Board member since 1996. Age 69.

Robert A. Elliott (2) (3) President and owner of The Elliott Accounting Group since 1983; Television Analyst/Pre-game Show Co-host for Fox Sports Arizona since 1999; Radio Host of "In the Paint" Sports Talk Show for KFNN 1490 AM from 2000 to 2002; Studio Expert Television Analyst for Cox Sports/Phoenix Suns from 1999 to 2001; Corporate Secretary of Southern Arizona Community Bank since 1999; Director and Minority Shareholder of Southern

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Arizona Community Bank since 1998; Director of Tucson Urban League since 1998; Treasurer of Tucson Urban League since 2002; Director of TEP since May 2003. Board member since 2003. Age 48.

Kenneth Handy (1) (2) (3) Retired CPA; Vice President and Chief Financial Officer of The Permanente Medical Group, Inc. (the physician services component of the Kaiser Permanente Medical Care Program in Northern California) from 1978 to 1998; Partner at Ernst & Ernst (now Ernst & Young) from 1972 to 1978; Director of TEP since 2001; Director of Millennium from 2001 to 2003. Board member since August 2001. Age 65.

Warren Y. Jobe (2) (3) (4) Retired CPA; Senior Vice President of Southern Company from 1998 to 2001; Executive Vice President and Chief Financial Officer and member of the Board of Directors of Georgia Power Company from 1982 to 1998; former President of the Georgia Power Foundation Inc. from 1986 to 2001; Member of the Board of Directors of Wellpoint Health Networks, Inc. since 2001; Director of TEP since 2001; Director of Millennium from 2001 to 2003. Board member since August 2001. Age 63.

- 
- (1) Member of the Corporate Governance and Nominating Committee.
  - (2) Member of the Audit Committee.
  - (3) Member of the Compensation Committee.
  - (4) Member of the Finance Committee.

The Board recommends that you vote "FOR" these nominees.

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BOARD INFORMATION

Board Meetings In 2003, the Board held a total of 13 regular and special meetings. Each director attended at least 75% of his or her Board and committee meetings.

Board Committees THE AUDIT COMMITTEE selects a firm of independent certified public accountants to audit annually our financial statements, reviews current and projected financial results of operations, reviews and discusses the scope of such audit, receives and reviews the audit reports and recommendations, transmits its recommendations to the Board, reviews our accounting and internal control procedures with our internal audit department from time to time and makes recommendations to the Board for any changes deemed necessary in such procedures, and performs such other functions delegated by the Board. Our Audit Committee held 12 meetings in 2003 and was in full compliance with its written charter.

Upon the recommendation of the Audit Committee, our Board adopted a code of ethics for our senior financial officers, including our Chief Executive Officer, Chief Financial Officer and Controller. A copy of this code of ethics can be obtained on our

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website at the following website address:  
<http://www.unisourceenergy.com>.

THE COMPENSATION COMMITTEE reviews the performance of our directors and officers and reviews and approves directors' and officers' compensation. Our Compensation Committee held six meetings in 2003 and was in full compliance with its written charter, which is attached to this Proxy Statement as Appendix A.

THE FINANCE COMMITTEE reviews and recommends to the Board long-range financial policies, objectives and actions required to achieve those objectives. Specifically, the Finance Committee reviews capital and operating budgets, current and projected financial results of operations, short-term and long-range financing plans, dividend policy, risk management activities and major commercial banking, investment banking, financial consulting and other financial relations of UniSource Energy. Our Finance Committee held three meetings in 2003.

THE CORPORATE GOVERNANCE AND NOMINATING COMMITTEE reviews and recommends corporate governance principles, interviews potential directors, and nominates and recommends to the shareholders and directors, as the case may be, qualified persons to serve as directors. The Corporate Governance and Nominating Committee also reviews and recommends membership for all the committees to the Board and reviews applicable rules and regulations relating to the duties and responsibilities of the Board. The Corporate Governance and Nominating Committee held four meetings in 2003 and was in full compliance with its written charter, which is attached to this Proxy Statement as Appendix B.

The Corporate Governance and Nominating Committee identifies and considers nominee candidates supplied by shareholders and Board members. The Corporate Secretary, as directed by the Corporate Governance and Nominating Committee, prepares portfolios for nominee candidates that include confirmation of the candidate's interest, independence, biographical information, review of business background and experience and reference checks. The Corporate Governance and Nominating Committee then evaluates candidates using, in large part, the criteria set forth in the next paragraph and any other criteria the Committee deems appropriate, and conducts a personal interview with each

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candidate. Upon completion of this process, formal invitations are extended to accept election to the Board.

The Corporate Governance and Nominating Committee has not adopted specific, minimum qualifications with

respect to a Committee-recommended Board nominee, but desirable qualifications are set forth in the Board manual and include prior community, professional or business experience that demonstrates leadership capabilities, the ability to review and analyze complex business issues, the ability to effectively represent the interests of our shareholders while keeping in perspective the interests of our customers, the ability to devote the time and interest required to attend and fully prepare for all regular and special Board meetings, the ability to communicate and work effectively with the other Board members and personnel and the ability to fully adhere to any applicable laws, rules or regulations relating to the performance of a director's duties and responsibilities.

While no formal policy exists, the Corporate Governance and Nominating Committee does consider recommendations for Board nominees received from our shareholders. The deadline for consideration of recommendations for next year's annual meeting of the shareholders is December 10, 2004 (assuming that the acquisition of UniSource Energy is not completed prior to such date). Recommendations must be in writing and include detailed biographical material indicating the candidate's qualifications and a written statement from the candidate of willingness and availability to serve. Recommendations should be directed to the Corporate Secretary, UniSource Energy Corporation, One South Church Avenue, Suite 1820, Tucson, Arizona 85701. In light of the acquisition of UniSource Energy, the Board does not believe it is appropriate to adopt a formal policy at this time.

Each member of our Audit Committee, Compensation Committee and Corporate Governance and Nominating Committee is independent based upon independence criteria established by our Board, which criteria is in compliance with applicable New York Stock Exchange listing standards.

#### BOARD COMPENSATION

Retainer and Fees	In 2003, each non-employee director received a \$20,000 annual cash retainer, \$1,000 for each Board meeting attended, \$1,000 for each committee meeting attended and an additional \$1,000 per committee meeting if acting as a committee chairperson. We reimburse directors for any expenses related to their Board and committee service.
Effect of Proposed Acquisition	See "Effect of Proposed Acquisition on Compensation" beginning on page 18 of this Proxy Statement for a discussion of the effect of the proposed acquisition of UniSource Energy on compensation of our Board members.

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Option and Restricted Share Grants Under the terms of the 1994 Outside Director Stock Option Plan, each non-employee director in office on the first business day of each year, and who has been a director for at least three months, is granted a stock option covering a number of shares of our common stock equal to \$10,000 divided by the value of an option as of the date of grant. Option values are determined using the Black Scholes option value model. The exercise price of the options is the fair market value of our shares on the grant date. The options vest in one-third increments on the grant date anniversary, and expire in ten years, provided, however, that all of these options will be cancelled and paid in cash upon the consummation of the acquisition.

Each non-employee director in office on the first business day of each year is granted a number of restricted shares of our common stock equal to \$10,000 divided by the then fair market value of a share of our common stock. Restricted shares vest on the third anniversary of the grant date, provided, however, that all shares subject to restricted stock awards outstanding will vest free of restrictions upon the consummation of the acquisition.

On January 2, 2003, each of the non-employee directors, with the exception of Mr. Elliott, received options to purchase 2,358 shares of our common stock at an exercise price of \$17.44, and 573 restricted shares of our common stock. Mr. Elliott received options to purchase 1,196 shares of our common stock at an exercise price of \$17.84 when he took office on May 9, 2003.

DIRECTOR COMPENSATION FOR LAST FISCAL YEAR

Name (1)	Cash Compensation		Number of Shares Subject to Restricted Stock Award
	Annual Retainer Fee (\$) (2)	Meeting Fees (\$) (2)	
Lawrence J. Aldrich	20,000	22,000 (3)	573
Larry W. Bickle	20,000	19,000 (3) (4)	573
Elizabeth T. Bilby	20,000	43,000	573
Harold W. Burlingame	20,000	42,000	573
John L. Carter	20,000	65,000 (3) (4)	573
Robert A. Elliott	15,000	35,000	--
Daniel W. L. Fessler (5)	15,000	19,000 (3)	573
Kenneth Handy	20,000	50,000	573
Warren Y. Jobe	20,000	61,000	573
H. Wilson Sundt (6)	6,666	16,000	573

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EXECUTIVE COMPENSATION AND OTHER INFORMATION

Summary of Compensation See "Effect of The Proposed Acquisition on Compensation" beginning on page 18 of this Proxy Statement for a discussion of the effect of the proposed acquisition of UniSource Energy and related shareholder approval on certain compensation of our executive officers.

The following table summarizes the compensation and stock option grants to, and stock options/stock appreciation rights ("SARs") held by the Named Executives.

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Annual Compensation		Restricted Stock Awards (\$)(1)	Se Un Opti
		Salary (\$)	Bonus (\$)		
James S. Pignatelli Chairman, President and Chief Executive Officer	2003	599,327	550,000	--	
	2002	574,654	320,000	--	1
	2001	559,423	580,000	--	1
Steven J. Glaser Senior Vice President and Chief Operating Officer, Transmission & Distribution - TEP	2003	274,596	166,000	--	
	2002	259,654	110,000	--	
	2001	244,231	132,000	--	
Dennis R. Nelson Senior Vice President and Chief Operating Officer - UES	2003	269,732	150,000	--	
	2002	260,000	90,000	--	
	2001	259,712	117,000	--	
Michael J. DeConcini Senior Vice President, Investments and Planning / Senior Vice President and Chief Operating Officer, Energy Resources - TEP	2003	229,192	145,000	--	
	2002	199,654	72,000	--	
	2001	184,519	97,125	--	
Kevin P. Larson Vice President, Chief Financial Officer and Treasurer	2003	219,462	145,000	--	
	2002	199,656	76,000	--	
	2001	184,519	113,000	--	
Vincent Nitido, Jr. Vice President, General Counsel and Chief Administrative Officer	2003	219,462	145,000	--	
	2002	199,654	68,000	--	
	2001	184,519	97,125	--	3

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Stock Option Grants in 2003 During 2003, the Compensation Committee of our Board granted stock options to officers. The options have exercise prices equal to the fair market value of our common stock at the date of grant, and were intended to be incentive stock options under, and to the maximum extent permitted by, the Internal Revenue Code of 1986, as amended ("Code"). These options would have vested ratably over a three-year period, provided, however, that all of these options vested and became immediately exercisable upon the approval of the acquisition agreement by our shareholders on March 29, 2004. The aggregate number of UniSource Energy shares attributable to the 2003 grants is 97,818.

The following table includes our 2003 grants of stock options and SARs to the Named Executives. The amounts shown as potential realizable values rely on arbitrarily assumed increases in value required by the SEC. In assessing those amounts, please note that the ultimate value of the options, as well as the shares, depends on actual future share prices. Market conditions and the efforts of the directors, the officers and others to foster the future success of UniSource Energy and its subsidiaries can influence those future share values.

OPTION/SAR GRANTS IN LAST FISCAL YEAR  
Individual Grants

Name	Number of Securities Underlying Options/SARs Granted	Percent of Total Options/SARs Granted to Employees in Fiscal Year	Exercise Price (\$/Sh)	Expiration Date
James S. Pignatelli	21,226	21.7%	17.84	5/9/13
Steven J. Glaser	9,729	9.9%	17.84	5/9/13
Dennis R. Nelson	9,552	9.8%	17.84	5/9/13
Michael J. DeConcini	8,137	8.3%	17.84	5/9/13
Kevin P. Larson	7,783	8.0%	17.84	5/9/13
Vincent Nitido, Jr.	7,783	8.0%	17.84	5/9/13

Option and SAR Holdings as of December 31, 2003 The following table includes the number and value of exercisable and non-exercisable options and SARs held by the Named Executives as of December 31, 2003.

AGGREGATED OPTION/SAR EXERCISES IN  
LAST FISCAL YEAR AND FISCAL YEAR-END OPTION/SAR VALUES

Number of Securities



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Name	Shares Acquired on Exercise (#)	Value Realized (\$)	Underlying Unexercised Options/SARs at Fiscal Year-End (#) Exercisable/Unexercisable (1)
James S. Pignatelli	--	--	435,629 / 279,559
Steven J. Glaser	--	--	132,143 / 57,729
Dennis R. Nelson	--	--	132,646 / 50,885
Michael J. DeConcini	--	--	63,881 / 71,469
Kevin P. Larson	--	--	69,386 / 37,782
Vincent Nitido, Jr.	--	--	68,811 / 72,782

2003 Long-Term Incentive Plan Awards

The following table includes the number of shares, units or other rights awarded to the Named Executives in the last fiscal year under any long-term incentive plan.

Payout of the 2003-2005 long-term incentive plan awards will be based on the achievement, during the performance period, of four (4) financial and two (2) operational goals, each on a UniSource Energy basis. The financial goals are total shareholder return, earnings per share, cash flow and equity capitalization. The operational goals are plant availability and customer measures. Each goal has an annual target, and each goal has an exceptional target for 2005. Two points are awarded for the achievement of each annual goal, and two additional points are awarded for achievement of each exceptional target for 2005. The payout will be based on cumulative points for the performance period. There are 48 available points. Threshold performance is achieved at 24 points, target performance at 30 points and maximum performance at 37 points.

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LONG-TERM INCENTIVE PLANS  
AWARDS IN LAST FISCAL YEAR

Name	Number of Shares, Units or Other Rights (#)	Performance or Other Period Until Maturity or Payout (3)	Estimated Future Pay Non-Stock Price-Bas Threshold (# or\$)	Target (# or\$)
James S. Pignatelli	18,370 (1) 189,000 (2)	1/1/03 - 12/31/05	7,564 \$78,000	18,370 \$189,000
Steven J. Glaser	8,420 (1)	1/1/03 - 12/31/05	3,467	8,420

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	87,000 (2)		\$36,000	\$87,000
Dennis R. Nelson	8,267 (1)	1/1/03 - 12/31/05	3,404	8,267
	85,000 (2)		\$35,000	\$85,000
Michael J. DeConcini	7,042 (1)	1/1/03 - 12/31/05	2,900	7,042
	72,000 (2)		\$30,000	\$72,000
Kevin P. Larson	6,736 (1)	1/1/03 - 12/31/05	2,774	6,736
	69,000 (2)		\$29,000	\$69,000
Vincent Nitido, Jr.	6,736 (1)	1/1/03 - 12/31/05	2,774	6,736
	69,000 (2)		\$29,000	\$69,000

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EQUITY COMPENSATION PLAN INFORMATION

Equity Compensation Plans Our only equity-based compensation plan that has not been approved by shareholders is the Management and Directors Deferred Compensation Plan (the "DCP"). Shareholder approval of the DCP has not been required. Under the DCP, certain eligible officers and other employees selected for participation, and non-employee members of the Board, may elect to defer a percentage of the compensation or fees that would otherwise become payable to the individual for their services to us. We also credit DCP accounts of employees participating in our 401(k) Plan with the additional amount of UniSource Energy matching contributions that the participant would have been entitled to under the 401(k) Plan if certain Code limits did not apply to limit the amount of UniSource Energy matching contributions made under the 401(k) Plan. Each participant in the DCP may elect that his or her deferrals be credited in the form of deferred shares. Deferred shares are bookkeeping entries that, when payable, will be paid in the form of an equivalent number of shares of UniSource Energy common stock. Deferred shares accrue dividend equivalents, credited in the form of additional deferred shares, as dividends are paid by UniSource Energy on its issued and outstanding common stock. Each participant elects the time and manner of payment (lump sum or installments) of his or her deferred shares under the DCP. The shares used to satisfy our stock obligations under the DCP are shares that have been purchased on the open market.

EQUITY COMPENSATION PLAN TABLE

The following table sets forth information as of December 31, 2003, with respect to UniSource Energy's equity compensation plans.

Number of Shares of

Number of Sh

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Plan Category	UniSource Energy Common Stock to be Issued Upon Exercise of Outstanding Options and Rights	Weighted-Average Exercise Price of Outstanding Options	Common Stock Future Compensation in t
Equity Compensation Plans Approved by Shareholders (1)	2,874,397 (2)	\$16.04 (3)	
Equity Compensation Plans Not Approved by Shareholders	60,203 (5)	--	
Total	2,934,600	--	

Pension Plans The following table shows the estimated annual retirement benefit payable to participants, including the Named Executives, for the average annual compensation and years of service indicated. Compensation is comprised of the officers' average annual compensation during the five consecutive years of employment with the highest compensation within the last 15 years preceding retirement. Compensation is comprised of salary and bonus, as shown on the Summary Compensation Table.

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PENSION PLAN TABLE

Remuneration (\$)	Years of Service			
	10	15	20	25
125,000	54,850	54,850	54,850	54,850
150,000	65,820	65,820	65,820	65,820
175,000	76,790	76,790	76,790	76,790
200,000	87,760	87,760	87,760	87,760
225,000	98,730	98,730	98,730	98,730
250,000	109,700	109,700	109,700	109,700
300,000	131,640	131,640	131,640	131,640
400,000	175,520	175,520	175,520	175,520
450,000	197,460	197,460	197,460	197,460
500,000	219,400	219,400	219,400	219,400
550,000	241,340	241,340	241,340	241,340
600,000	263,280	263,280	263,280	263,280
650,000	285,220	285,220	285,220	285,220
700,000	307,160	307,160	307,160	307,160
750,000	329,100	329,100	329,100	329,100
800,000	351,040	351,040	351,040	351,040
850,000	372,980	372,980	372,980	372,980
900,000	394,920	394,920	394,920	394,920
950,000	416,860	416,860	416,860	416,860
1,000,000	438,800	438,800	438,800	438,800
1,100,000	482,680	482,680	482,680	482,680
1,200,000	526,560	526,560	526,560	526,560

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1,300,000	570,440	570,440	570,440	570,440	570
1,400,000	614,320	614,320	614,320	614,320	614

The amount of the pension benefit is equal to a base of 40% of the compensation for ten years of service, plus 9.7% (life annuity factor) of such calculated amount. The estimated benefits shown in the Pension Plan Table are straight life annuities not subject to a reduction for any Social Security benefits. The table also reflects amounts payable under the Excess Benefits Plan which will pay from the general funds of UniSource Energy the difference, if any, between the benefits under TEP's pension plan and any benefit payments, which may be limited by federal regulations.

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The credited years of service for UniSource Energy's Named Executives are as follows:

Name ----	Credited Years of Service -----
James S. Pignatelli	9
Steven J. Glaser	14
Dennis R. Nelson	26
Kevin P. Larson	18
Michael J. DeConcini	15
Vincent Nitido, Jr.	13

EFFECT OF PROPOSED ACQUISITION ON COMPENSATION

New Employment Arrangements	As of the date of this Proxy Statement, no member of our management has entered into any amendments or modifications to existing employment agreements with us or our subsidiaries in anticipation of the acquisition. Nor has any member of our management entered into any agreement, arrangement or understanding with Saguaro Utility or its affiliates regarding employment with, or the right to purchase or participate in the equity of, the surviving corporation. Although no such agreement, arrangement or understanding currently exists, it is generally expected that our existing management will remain after the acquisition is completed, which means that members of our existing management may, prior to the closing of the acquisition, enter into new arrangements with Saguaro Utility or its affiliates regarding employment with, or the right to purchase or participate in the equity of, the surviving corporation.
Change in Control Agreements	TEP has Change in Control Agreements ("Agreements") with all of its officers. The Agreements are in effect until the later of: (i) five

Change in  
Control Agreements  
were adopted  
to attract  
and retain  
quality management.

years after the date either TEP or the officer gives written notice of termination of the Agreement, or (ii) if a change in control occurs during the term of the Agreement, five years after the change in control. On March 29, 2004, upon the approval of the acquisition agreement by our shareholders, a change in control occurred for purposes of the Agreements. This will be true irrespective of whether or not the acquisition is completed.

The Agreements provide that each officer shall be employed by TEP, or one of its subsidiaries or affiliates, in a position comparable to his or her current position, with compensation and benefits, which are at least equal to their then current compensation and benefits, for a period of five years after a change in control (subject to earlier termination due to the officer's acceptance of a position with another company or termination for cause).

In the event that the officer's employment is terminated by TEP (with the exception of termination due to the officer's acceptance of another position or for cause), or if the officer terminates employment because of a reduction in position, responsibility, compensation or for certain other stated reasons, the officer is entitled to severance benefits in the form of: (i) a lump sum payment equal to the present value of three times annual salary and bonus compensation; (ii) the present value of the additional amount the officer would have received under the TEP Retirement Plan if the officer had continued to be employed for the five-year period after a change in control occurs; plus (iii) the present value of any employee awards under the 1994 Omnibus Stock and Incentive Plan or any

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successor plan, which are outstanding at the time of the officer's termination (whether vested or not), prorated based on length of service. Such officer is also entitled to continue to participate in TEP's health, death and disability benefit plans for five years after the termination. The Agreements further provide that TEP will make a payment to the officer to offset any excise taxes that may become payable under certain conditions. Any payments made in respect of such excise taxes are not deductible by us. Assuming Mr. Pignatelli's and the other Named Executives' employment was terminated, the total payments made by UniSource Energy pursuant to the Agreements would not be expected to exceed \$17 million.

Treatment of  
Stock Options

Our Board has over time granted options to our executive officers and managers that allow those individuals to purchase our common stock at fair

market value on the date of issuance. Members of our Board have also over time received grants of options to purchase our common stock at specified prices. On March 29, 2004, upon the approval of the acquisition agreement by our shareholders, a change of control occurred for purposes of the outstanding stock options under the UniSource Energy Corporation 1994 Omnibus Stock and Incentive Plan, with the effect of making all outstanding stock options of officers and managers immediately exercisable. Upon consummation of the acquisition, all outstanding stock options under the UniSource Energy Corporation 1994 Outside Director Stock Option Plan will become immediately exercisable by members of our Board. In connection with the acquisition agreement, Saguaro Utility, through its affiliate, has agreed to pay at the effective time of the acquisition, with respect to all outstanding options, an amount in cash equal to the product of:

- o the total number of shares of our common stock underlying a holder's options, and
- o the excess of \$25.25 over the exercise price per share of the shares of our common stock underlying such options.

Due to this provision, as of the Record Date, our Board members and the Named Executives listed in the chart that immediately follows this paragraph will be entitled to receive, at the effective time of the acquisition, the following cash payments, respectively, with respect to the cancellation of their options (assuming that the options outstanding as of the Record Date are not exercised or canceled prior to the effective time):

Name and Title -----	Amount (1) -----
James S. Pignatelli Chairman, President and Chief Executive Officer	\$6,790,211
Lawrence J. Aldrich Director	\$66,268
Larry W. Bickle Director	\$109,306
Elizabeth T. Bilby Director	\$139,568

Name and Title -----	Amount (1) -----
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Harold W. Burlingame Director	\$109,306
John L. Carter Director	\$127,868
Robert A. Elliott Director	\$8,862
Kenneth Handy Director	\$48,636
Warren Y. Jobe Director	\$48,636
Steven J. Glaser Senior Vice President and Chief Operating Officer, Transmission & Distribution -TEP	\$1,697,485
Dennis R. Nelson Senior Vice President and Chief Operating Officer - UES	\$1,716,325
Michael J. DeConcini Senior Vice President, Investments and Planning / Senior Vice President and Chief Operating Officer, Energy Resources - TEP	\$1,220,738
Kevin P. Larson Vice President, Chief Financial Officer and Treasurer	\$979,258
Vincent Nitido, Jr. Vice President, General Counsel and Chief Administrative Officer	\$1,269,188
All directors and executive officers as a group	\$17,960,593

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Treatment of Other Compensation	As discussed under "Equity Compensation Plan Information" on page 15 of this Proxy Statement, we maintain a deferred compensation plan that permits officers and directors to defer a percentage of the compensation or fees that would otherwise be payable to the individual for their services to us. A participant in this plan may elect that his or her deferrals be credited in, among other things, the form of a deemed investment in shares of our common stock. A trust has been established that maintains a position in our common stock corresponding to the plan participants' deemed investment in our common stock. Distributions are made in stock or cash, at our discretion. In addition, our Board has, over time, granted our executive officers and managers restricted stock units under our stock and incentive plans. Upon vesting, officers and managers may defer receipt of these restricted stock unit awards, in which case, the deferred awards are
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credited to a bookkeeping account in the form of dividend equivalent-bearing stock units. The table that follows sets forth the allocable amount of shares of common stock credited to our directors and the Named Executives as of the Record Date with respect to the deferred compensation plan and dividend equivalent-bearing stock units.

Our Board has also, over time, granted our executive officers and managers other equity-based compensation awards, including performance shares and performance units under our stock and incentive plans. Performance shares are distributed as shares of our common stock, and performance units are distributed as cash, in each case, when, and to the extent, that performance goals during a specified performance period have been met. On March 29, 2004, upon the approval of the acquisition agreement by our shareholders, a change of control occurred for purposes of these awards and the awards fully vested, at target. See "2003 Long-Term Incentive Plan Awards" on page 14 of this Proxy Statement. As provided in the following table, upon the change of control, all shares of common stock were distributed with respect to performance shares and all cash payments were made with respect to performance units.

Name and Title -----	Allocable Amount of Deferred Shares -----	Number of Perform Issued/Amount of Respect to Perfo -----
James S. Pignatelli Chairman, President and Chief Executive Officer	137,385	12,675 / \$
Lawrence J. Aldrich Director	1,548	--
Larry W. Bickle Director	405	--
Elizabeth T. Bilby Director	4,378	--
Harold W. Burlingame Director	1,548	--
John L. Carter Director	10,338	--
Robert A. Elliott Director	405	--
Kenneth Handy Director	3,438	--



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Warren Y. Jobe Director	1,548	--
Steven J. Glaser Senior Vice President and Chief Operating Officer, Transmission & Distribution - TEP	29,574	5,809 / \$1

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Name and Title -----	Allocable Amount of Deferred Shares -----	Number of Perfor Issued/Amount of Respect to Perfo -----
Dennis R. Nelson Senior Vice President and Chief Operating Officer - UES	26,353	5,704 / \$1
Michael J. DeConcini Senior Vice President, Investments and Planning / Senior Vice President and Chief Operating Officer, Energy Resources - TEP	24,307	4,858 / \$1
Kevin P. Larson Vice President, Chief Financial Officer and Treasurer	774	3,770 / \$1
Vincent Nitido, Jr. Vice President, General Counsel and Chief Administrative Officer	16,470	3,770 / \$1
All directors and executive officers as a group	302,686	53,566 / \$1

DIRECTOR INDEPENDENCE CRITERIA

Board independence is determined by consideration of established criteria. The Board has established the following criteria for determining independence, including for the purpose of serving upon the Audit Committee, the Compensation Committee and the Corporate Governance and Nominating Committee.

Directors that meet each of the following criteria are deemed independent:

1. A director who is a former employee of UniSource Energy cannot be "independent" until five years after employment has ended, provided, however, that a director who serves as an interim Chairman or CEO is excluded from the definition of a "former employee" and thus deemed independent immediately after his or her service as interim Chairman or CEO ends.

2. A director who is, or in the past five years has been, affiliated with or employed by a (present or former) auditor of UniSource Energy (or of an affiliate) cannot be "independent" until five years after the end of either the affiliation or the auditing relationship.
3. A director cannot be "independent" if he or she is, or in the past five years has been, part of an interlocking directorate in which an executive officer of UniSource Energy serves on the compensation committee of another company that concurrently employs the director.
4. Directors with immediate family members in the foregoing categories (items 1-3) are likewise subject to the five-year "cooling-off" provisions for purposes of determining "independence," provided, however, that employment of a family member in a non-officer position does not preclude a director from being deemed "independent."

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5. A director who possesses an interest in any transaction for which disclosure would be required pursuant to Item 404(a) of SEC Regulation S-K (generally, this item requires proxy statement disclosure of transactions exceeding \$60,000 between a director and UniSource Energy or any of our subsidiaries) cannot be independent.
6. Directors that do not meet item 5 of the aforementioned criteria may nonetheless be deemed independent by a majority of independent directors, provided the basis for such determination shall be disclosed in our Proxy Statement.

Based upon the foregoing criteria, the Board has deemed each director to be independent, with the exception of Lawrence J. Aldrich and Larry W. Bickle. See "Transactions with Management and Others" below.

#### TRANSACTIONS WITH MANAGEMENT AND OTHERS

Haddington  
Energy  
Partners II LP

Millennium was authorized by its Board of Directors in 2000 to invest \$15 million, in aggregate, over a three- to five-year period in Haddington Energy Partners II LP. Mr. Bickle, a member of our Board, is the managing director of Haddington Ventures LLC, the general partner of Haddington Energy Partners II LP. As of December 31, 2003, Millennium had funded approximately \$8.5 million under this commitment, \$2.4 million of which was funded in 2003.

Valley Ventures III, LP Millennium made a commitment of \$5 million capital plus a share of expenses to Tucson Ventures, LLC, a venture capital fund, in 2000. Tucson Ventures, LLC merged with Valley Ventures III, LP, also a venture capital fund, in 2002. In connection with the merger of the funds, Millennium's commitment was revised to a total of \$6 million, including expenses. Mr. Aldrich, a member of our Board, is a general partner of the company that manages Valley Ventures III, LP. As of December 31, 2003, Millennium had funded approximately \$1.2 million under this commitment.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

Millennium Energy Investments Mr. Stephen Alexander, an immediate family member of Mrs. Bilby, a member of our Compensation Committee, is employed by Millennium. As Director of Energy Investments, Mr. Alexander assists in overseeing Millennium's investment portfolio. For his services in 2003, Mr. Alexander received compensation of approximately \$150,000 from Millennium.

COMPENSATION COMMITTEE REPORT ON EXECUTIVE COMPENSATION

The Committee The Compensation Committee is responsible for developing and administering executive compensation policies and programs for UniSource Energy and TEP and making recommendations to the Board with respect thereto. The Compensation Committee makes recommendations to the Board with respect to the compensation of UniSource Energy's executive officers, including Mr. Pignatelli and the other Named Executives, and sets policies for and reviews the compensation awarded to other key members of management. UniSource Energy applies a consistent philosophy to compensation for all executive employees, including the Named Executives.

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Overall Objectives UniSource Energy's executive compensation policies and programs generally are intended to (i) relate the compensation of employees to the success of UniSource Energy and the corresponding creation of shareholder value, and (ii) attract, retain and motivate executives and key employees with competitive compensation opportunities.

Executive Compensation Generally The Compensation Committee reviews our executives' compensation each year. Compensation depends on many factors, including individual performance, responsibilities, future challenges and objectives and the executive's potential contribution to our future success. The Compensation Committee also looks at our financial performance and the compensation levels at comparable companies.

UniSource Energy's 2003 compensation program consisted

of three components:

- o base salary;
- o short-term incentive compensation; and
- o long-term incentive compensation.

Base Salary The base salary component of compensation is intended to be competitive with that paid by comparable companies in the energy industry. In developing the compensation program, the Compensation Committee retained an external consultant to conduct a competitive analysis of pay for UniSource Energy's officer group. In conducting its analysis for 2003, the consultant selected a peer group of energy companies with a revenue range of \$264 million to \$6 billion. UniSource Energy ranks at the 37th percentile of the peer group. Twenty-one of the 25 peer group companies have both regulated utility and non-regulated energy businesses. The Compensation Committee believes the companies in the comparator group are a more appropriate comparison for UniSource Energy than the Edison Electric 100 companies used in the Performance Graph on page 28 of this Proxy Statement, because the type of business and annual revenues of the companies included in the survey are more closely related to those of UniSource Energy and the companies in the comparator group represent primary competitors to UniSource Energy for top-level management personnel. The external data from companies in the comparator group was used to develop market compensation for each executive position. "Market compensation" refers to the median salary for executives in the comparator group. Base salaries for UniSource Energy's executive officers, including Mr. Pignatelli and the other Named Executives, were set at market compensation levels in January 2003, in recognition of the increasingly competitive environment in the electric industry, the need to continue to attract and retain highly qualified executives and the fact that a substantial portion of each executive's total compensation package is "at-risk," based on the achievement of certain corporate goals. See "Short-Term Incentive Compensation and Long-Term Incentive Compensation" below.

Short-Term Incentive Compensation The Board adopted a Short-Term Incentive Plan to provide compensation for meeting or exceeding specified objectives designed to contribute to the attainment of UniSource Energy's performance targets and long-term strategic plan. Under the Short-Term Incentive Plan, target award levels are set as a percentage of each participant's base salary. In 2003, the target award levels for our executive officers ranged from 30% to 70% of base salary. Awards for Mr. Pignatelli and the remaining executive officers are determined by the Board

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based on the accomplishment of previously established individual goals and contribution to business results. Based on the foregoing factors, the Compensation Committee made awards to the Named Executives ranging from 56% to 92% of base salary. Incentive compensation awarded to Mr. Pignatelli and the other Named Executives is set forth in the preceding Summary Compensation Table.

Long-Term Incentive Compensation      UniSource Energy's long-term incentive compensation is intended to attract and retain quality employees over the long-term in a manner that directly aligns them with shareholder interest.

At the recommendation of the Compensation Committee, the Board unanimously adopted and, at the 1994 annual meeting of the shareholders, the shareholders approved the Tucson Electric Power Company (now UniSource Energy) 1994 Omnibus Stock and Incentive Plan. On May 9, 2003, the Compensation Committee issued stock options (intended to be incentive stock options), performance shares (denominated in shares) and performance units (denominated in cash) to all executive officers of UniSource Energy, including Mr. Pignatelli and the other Named Executives. In calculating the level of awards to the executive officers, the Compensation Committee considered the above analysis of executive compensation for comparative companies. Based on such analysis, the Compensation Committee awarded Mr. Pignatelli and the other Named Executives stock options, performance shares and performance units with a total value equal to 100% of base salary for target performance. The number of UniSource Energy shares covered by the stock option grant to Mr. Pignatelli was 21,226, the number of performance shares was 18,370, and the number of performance units was 189,000. See "2003 Long-Term Incentives Plan Awards" on page 14 of this Proxy Statement for a discussion of the performance criteria upon which the payout of performance shares and performance units is dependent. In determining the 2003 long-term incentive awards, the Compensation Committee did not consider the number of options previously granted or outstanding.

Tax Code Concerns      The Compensation Committee does not presently have a policy regarding qualifying compensation paid to executive officers for deductibility under Section 162(m) of the Code.

Respectfully submitted,

THE COMPENSATION COMMITTEE

H. Wilson Sundt, Chair (1/03-5/03)  
Harold W. Burlingame, Chair (6/03-12/03)  
Elizabeth T. Bilby  
John L. Carter  
Robert A. Elliott

Kenneth Handy  
Warren Y. Jobe

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AUDIT COMMITTEE REPORT

The Committee      The Audit Committee is made up of five financially literate directors who are independent based upon independence criteria established by our Board, which criteria is in compliance with applicable New York Stock Exchange listing standards. Our Board has determined that each member of the Audit Committee has accounting and/or related financial management expertise and as such has not designated any single Audit Committee member as the Audit Committee "financial expert." However, our Board anticipates that it will formally designate one member of the Audit Committee to be the Audit Committee "financial expert" at its May 2004 Board meeting. The Board previously adopted a written charter for the Audit Committee. The Committee has complied with its charter, including the requirement to meet periodically with our independent auditors, internal audit department and management to discuss the auditors' findings and other financial and accounting matters.

In connection with our December 31, 2003 financial statements, the Audit Committee has (i) reviewed and discussed the audited financial statements with management; (ii) discussed with PricewaterhouseCoopers, LLP, our independent auditor, the matters required to be discussed by SAS 61 (Codification of Statements on Auditing Standards, AU Sec. 380); (iii) received from PricewaterhouseCoopers, LLP the written disclosures and the letter required by Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees); and (iv) discussed with PricewaterhouseCoopers, LLP its independence.

Based on all of its activities during the year, the Audit Committee recommended to the Board that the audited financial statements for 2003 be included in the Annual Report on Form 10-K for filing with the SEC.

Pre-Approved Policies and Procedures      Rules adopted by the SEC in order to implement requirements of the Sarbanes-Oxley Act of 2002 require public company audit committees to pre-approve audit and non-audit services. Our Audit Committee has adopted a policy pursuant to which audit, audit-related, tax and other services are pre-approved by category of service. Recognizing that situations may arise where it is in our best interest for the auditor to perform services in addition to the annual audit of our financial statements, the policy sets forth guidelines and procedures with respect to approval of the four categories of service

designed to achieve the continued independence of the auditor when it is retained to perform such services for us. The policy requires the Audit Committee to be informed of each service and does not include any delegation of the Audit Committee's responsibilities to management. The Audit Committee may delegate to the Chairman of the Audit Committee the authority to grant pre-approvals of audit and non-audit services requiring Audit Committee approval where the Audit Committee Chairman believes it is desirable to pre-approve such services prior to the next regularly scheduled Audit Committee meeting. The decisions of the Audit Committee Chairman to pre-approve any such services from one regularly scheduled Audit Committee meeting to the next shall be reported to the Audit Committee.

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Fees The following table details fees paid to PricewaterhouseCoopers, LLP for professional services during 2002 and 2003. The Audit Committee has considered whether the provision of services to us by PricewaterhouseCoopers, LLP, beyond those rendered in connection with their audit and review of our financial statements, is compatible with maintaining their independence as auditors.

	2002 ----	2003 ----
Audit Fees	\$821,739	\$1,030,4
Audit-Related Fees	\$194,989	\$713,4
Tax Fees	\$62,453	\$55,4
All Other Fees	\$39,812	\$2,5

Fees for audit services include fees for the audit of our consolidated financial statements included in our Annual Report on Form 10-K and review of financial statements included in our quarterly reports on Form 10-Q, comfort letters, consents and other services related to SEC matters and financing transactions, statutory and regulatory audits, and accounting consultations to the extent necessary for PricewaterhouseCoopers, LLP to fulfill their responsibilities under generally accepted auditing standards. Audit-related fees principally include accounting and electric system assets from Citizens Communications Company on August 11, 2003 and due diligence related to the Springerville expansion and proposed acquisition of UniSource Energy by an affiliate of Saguaro Utility. Tax fees include tax compliance, tax advice, and tax planning. All other fees principally include accounting training. Amounts previously reported for 2002 have been reclassified to conform to the categories required for 2003.

Respectfully submitted,

THE AUDIT COMMITTEE

Warren Y. Jobe, Chair  
 Elizabeth T. Bilby  
 John L. Carter  
 Robert A. Elliott  
 Kenneth Handy

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PERFORMANCE GRAPH

Comparison of Cumulative Five-Year Total Return Among  
 UniSource Energy, Standard & Poor's 500 Index  
 and EEI Index of 64 Investor-Owned Utilities (1)

The graph showing on the hard copy represents the comparison of four year cumulative total return between UniSource Energy Corporation, the S&P 500 Index, and EEI Index of 100 investor-owned utilities. The graph's X-axis shows the years 1998 to 2003, and the Y-axis shows dollar values from zero to 250. The data points are connected by lines with the following markers: UniSource Energy Corporation - triangles; S&P 500 - diamonds; EEI Index - 100 Electrics - squares. The data points are as follows:

	1998	1999	2000	2001	2002	2003
	----	----	----	----	----	----
UniSource Energy Corporation	\$100	\$83	\$142	\$141	\$137	\$202
S&P 500 Index	\$100	\$121	\$120	\$110	\$76	\$97
EEI Index - 100 Electrics	\$100	\$81	\$110	\$97	\$94	\$116

Data and Calculations	1999	2000	2001	2002
-----	----	----	----	----
S&P 500 Total Return Change	21.04%	-9.10%	-11.89%	-22.10%
EEI Index - 64 Electrics Change	-18.60%	47.97%	-8.79%	-14.73%
UniSource Energy Change	-17.13%	71.80%	-1.30%	-2.20%

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SUBMISSION OF SHAREHOLDER PROPOSALS

General Rule 14a-4 of the SEC's proxy rules allows us to use discretionary voting authority to vote on a matter coming before an annual meeting of our shareholders, which was not included in our Proxy Statement (if we do not have notice of the matter at least 45 days before the date on which we first mailed our proxy



materials for the prior year's annual meeting of the shareholders). In addition, we may also use discretionary voting authority if we receive timely notice of such matter (as described in the preceding sentence) and if, in the Proxy Statement, we describe the nature of such matter and how we intend to exercise our discretion to vote on it. Accordingly, for our 2005 annual meeting of shareholders, any such notice must be submitted to the Corporate Secretary of UniSource Energy on or before February 24, 2005 (assuming that the acquisition of UniSource Energy is not completed prior to such date).

We must receive your shareholder proposals by December 10, 2004.

This requirement is separate and apart from the SEC's requirements that a shareholder must meet in order to have a shareholder proposal included in our Proxy Statement. Shareholder proposals intended to be presented at our 2005 annual meeting of the shareholders (assuming that the acquisition of UniSource Energy is not completed prior to our 2005 annual meeting of shareholders) must be received by us no later than December 10, 2004 (assuming that the acquisition of UniSource Energy is not completed prior to such date), in order to be eligible for inclusion in our Proxy Statement and the form of proxy relating to that meeting. Direct any proposals, as well as related questions, to the undersigned.

OTHER BUSINESS

The Board knows of no other matters for consideration at the Meeting. If any other business should properly arise, the persons appointed in the enclosed proxy have discretionary authority to vote in accordance with their best judgment.

Copies of our 2003 Annual Report on Form 10-K may be obtained by shareholders, without charge, upon written request to Library and Resource Center, UniSource Energy Corporation, 3950 East Irvington Road, Mail Stop RC114, Tucson, Arizona 85714. You may also obtain our SEC filings through the Internet at [www.sec.gov](http://www.sec.gov) or [www.UniSourceEnergy.com](http://www.UniSourceEnergy.com).

By order of the Board of Directors,  
/s/ Catherine A. Nichols

-----  
Catherine A. Nichols  
Corporate Secretary

PLEASE VOTE - YOUR VOTE IS IMPORTANT

UNISOURCE ENERGY CORPORATION  
COMPENSATION COMMITTEE OF THE BOARD OF DIRECTORS  
CHARTER

1. COMPOSITION

The Compensation Committee of the Board of Directors consists of not fewer than three Directors appointed annually by the Board. All members of the Committee shall be determined to be independent in accordance with the NYSE Listed Company Manual. The Board shall designate one of the Committee members as Chairman of the Committee.

2. MEMBER QUALIFICATIONS

A Director shall be qualified to serve on the Committee if he or she qualifies as independent under the NYSE Listed Company Manual.

3. MEMBER APPOINTMENT AND REMOVAL

All members of the Committee shall be appointed and/or removed by the Corporate Governance & Nominating Committee.

4. MEETINGS

The Committee will hold at least three regular meetings each year, and such additional meetings, as it may deem necessary. In addition to the Committee members and the Secretary, the Chairman of the Board, Chief Executive Officer and President and other members of management may attend as is appropriate.

5. RULES OF PROCEDURE

The Committee will determine its own rules of procedure with respect to how its meetings are to be called, as well as the place, time and frequency. In the absence of such rules, the Committee will meet at the call of its Chairman as is required to accomplish the purposes of the Committee.

6. COMPENSATION

Each member will be paid for each meeting attended the same fee paid for attendance at other Committee meetings of the Board, and will be reimbursed for travel expenses incurred by attendance at meetings.

7. COMMITTEE SECRETARY

The Secretary of the Committee will be the Asst. Corporate Secretary of the Company (or such other officer as the Committee may designate) and not be a member of the Committee. The Secretary will attend all meetings and maintain minutes, advise members of all meetings called, arrange with the Chairman or other convening authority for preparation and distribution of the agenda for each meeting, and carry out other functions as may be assigned from time to time by the Committee. At such meetings where attendance by a Company officer is not appropriate, the Chairman shall act as secretary of the meeting or appoint another member of the Committee to act as secretary of such meetings.

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### 8. QUORUM

A majority of the total membership of the Committee will constitute a quorum.

### 9. RESPONSIBILITIES

The function of the Committee is to assure an internally consistent and externally competitive executive compensation program in order to attract, motivate and retain qualified executives. It is also the Committee's function to provide incentives for the attainment of the Company's strategic goals and objectives and to produce a report on executive compensation for inclusion in the Proxy Statement of the Company.

For purposes of the Committee's responsibilities, executives are defined as all officers of the Company.

### 10. SPECIFIC DUTIES OF THE COMMITTEE

1. Approve the compensation philosophy and guidelines for the executive group, including base salary structure, incentive compensation, and long range strategic incentive programs to attract, retain and motivate executives.
2. Review and approve corporate goals and objectives relating to CEO compensation.
3. Evaluate CEO performance in light of corporate goals and objectives and set CEO compensation level based upon evaluation of the performance of such goals and objectives.
4. Review and approve, based on reviews of compensation practices in related and other industries, the appropriate compensation levels including fringes and other benefits for the CEO.
5. Receive the CEO's recommendations, review and approve compensation for all of the Company's executives, including any equity compensation awarded, fringes and other benefits, and the ability to delegate action to Management in conjunction with the aforementioned compensation.
6. Review and approve any management incentive plans, including the participants, goals, payout ratios, etc., which involve executives of the Company.
7. Administer the Company's long range incentive plan, including selection of participants, setting of objectives, and determination of awards, as more fully defined in such plan. Recommend changes to the long range incentive program as deemed necessary considering the Company's performance, relative shareholder return, value of similar awards at similar companies and awards given to the Company's CEO in past years.
8. Review and approve any special employment contract or other special agreement, such as a supplementary pension agreement, for any of the Company's executives.
9. Produce an annual report, in accordance with applicable rules

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and regulations, on executive compensation for inclusion in the proxy statement.

10. Periodically, receive a briefing by management regarding the administration and appropriateness of the total rewards package including base, short-term and long-term compensation and health and welfare plans, for non-executive employees.
11. Review and approve Director compensation, including short- and long-term incentives.

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12. Review and approve policy for reimbursement of Director expenses.
13. As necessary, carry out other duties assigned by the Board to the Committee that are related to compensation and management development.
14. Retain and terminate any consulting firms to be used to assist in the evaluation of director, CEO or executive compensation. This authority shall be exclusive to this Committee.
15. Annually review its performance as a Committee.

### 11. RESPONSIBILITIES OF THE CHAIRMAN

The Chairman of the Committee will present the Committee's recommendations to the Board for its approval and periodically provide the Board, for its information, with a summary of the Committee's determinations and approvals.

### 12. RESPONSIBILITIES OF THE CHIEF EXECUTIVE OFFICER

The Chief Executive Officer of the Company will advise and make recommendations to the Committee and, in the normal course, attend all meetings of the Committee, with the exception of that portion of any meeting where compensation of the Chief Executive Officer is considered. It is also the responsibility of the Chief Executive Officer to coordinate the implementation and execution of Committee determinations.

### 13. OTHER AUTHORITY

The Committee may call upon any person including employees of the Company or its subsidiaries, knowledgeable in matters discussed by the Committee, for information and counsel.

### 14. ANNUAL SCHEDULE

The routine business of the Committee shall be considered in accordance with the Annual Schedule attached as Exhibit A.

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EXHIBIT A

11/03

COMPENSATION COMMITTEE ANNUAL SCHEDULE

February	Review prior year performance under short term incentive program and determine awards
	Review current year Performance Enhancement Plan
	Approve report of Committee for inclusion in Proxy
August	Meet with consultant re upcoming review of Director and Officer compensation
October	Review of compensation for Directors and Officers
December	Establish director retainer and meetings fees to be effective January 1st of following year.
	Establish Officer compensation for following year.
	Review corporate goals and objectives for following year

(The dates on the above schedule are subject to change.)

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APPENDIX B  
February 5, 2004

UNISOURCE ENERGY CORPORATION

CORPORATE GOVERNANCE AND NOMINATING COMMITTEE OF THE BOARD OF DIRECTORS

CHARTER

1. COMPOSITION

The Corporate Governance and Nominating Committee of the Board of Directors (the "Committee") consists of not fewer than three Directors appointed annually by the Board. All members of the Committee shall be determined to be independent in accordance with the NYSE Listed Company Manual. The Board shall designate one of the Committee members as Chairman of the Committee.

2. QUALIFICATIONS

A Director shall be qualified to serve on the Committee if he or she

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qualifies as independent under the Company's Director Independence Criteria.

### 4. APPOINTMENT AND REMOVAL OF COMMITTEE MEMBERS

All members of the Committee shall be appointed and/or removed by the Board of Directors.

### 5. MEETINGS

The Committee will meet regularly to prepare for any upcoming vacancies on the Board of Directors and to address corporate governance. In addition to the Committee members and the Secretary, the Chairman of the Board, Chief Executive Officer and President and other members of the Board and management may attend as appropriate.

### 6. RULES OF PROCEDURE

The Committee will determine its own rules of procedure with respect to how its meetings are to be called, as well as the place, time and frequency. In the absence of such rules, the Committee will meet at the call of its Chairman as is required to accomplish the purposes of the Committee.

### 7. COMPENSATION

Each member will be paid such fees as may be established from time to time by the Board for service on the Committee, and will be reimbursed for travel expenses incurred by attendance at meetings.

### 8. COMMITTEE SECRETARY

The Secretary of the Committee will be the Asst. Corporate Secretary of the Company (or such other representative of management as the Committee may designate) and will not be a member of the Committee. The Secretary will attend all meetings and maintain minutes, advise members of all meetings called, arrange with the Chairman or other convening authority for preparation and distribution of the agenda for each meeting, and carry out other functions as may be assigned from time to time by the Committee. At such

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meetings where attendance by a Company representative is not appropriate, the Chairman shall act as secretary of the meeting or appoint another member of the Committee to act as secretary of such meetings.

### 9. QUORUM

A majority of the total membership of the Committee will constitute a quorum.

### 10. RESPONSIBILITIES AND SPECIFIC DUTIES OF THE COMMITTEE

The functions of the Committee shall be:

1. Regularly review and assess the current Board membership as to size, skills and upcoming vacancies.

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2. Make recommendations to the Board with respect to desired background, skill sets, experience and characteristics of Board members, as well as continuing education, conferences and seminars that Directors might attend to enhance their skill sets.
  3. Regularly review and/or update the Candidate Evaluation Form.
  4. Fill vacancies on Board of Directors by gathering and reviewing information on potential Board members; interviewing potential Board candidates; and, recommending potential Board members to the Board of Directors.
  5. Review and approve all UniSource Board committee members and board members of major subsidiaries.
  6. Annually review and recommend for approval corporate governance principles.
  7. Facilitate periodic evaluation of the Board's collective performance.
  8. Annually evaluate the performance of this Committee.
  9. To retain and terminate any search firms to be used to identify director candidates including any terms of retention. This authority shall be exclusive to this Committee.
  10. Annually review and approve modifications to the Company Board Manual.
11. RESPONSIBILITIES OF THE CHAIRMAN
- The Chairman of the Committee will present the Committee's recommendations to the Board for its approval and periodically provide the Board, for its information, with a summary of the Committee's determinations and approvals.
12. RESPONSIBILITIES OF THE CHIEF EXECUTIVE OFFICER
- The Chief Executive Officer of the Company will advise and make recommendations to the Committee and, in the normal course, attend all meetings of the Committee.
13. OTHER AUTHORITY
- The Committee may call upon any person including employees of the Company or its subsidiaries, knowledgeable in matters discussed by the Committee, for information and counsel.

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APPENDIX B  
FORM OF PROXY CARD

UNISOURCE ENERGY  
YOUR VOTE IS IMPORTANT

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VOTE BY TELEPHONE OR INTERNET  
24 HOURS A DAY - 7 DAYS A WEEK

INTERNET

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<https://www.proxyvotenow.com/uns>

- Go to the website address listed above.
- Have your proxy card ready.
- Follow the simple instructions that appear on your computer screen.

OR

TELEPHONE

-----

1-866-358-4695

- Use any touch-tone telephone.
- Have your proxy card ready.
- Follow the simple recorded instructions.

OR

MAIL

----

- Mark, sign and date your proxy card.
- Detach your proxy card.
- Return your proxy card in the postage-paid envelope provided.

You can vote your shares by telephone, the Internet, mail or in person at the Annual Shareholders' Meeting. Your telephone or Internet vote authorizes the named proxies to vote your shares in the same manner as if you marked, signed and returned your proxy card. If you have submitted your proxy by the Internet or telephone there is no need to mail your proxy card.

1-866-358-4695

CALL TOLL-FREE TO VOTE

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THE INTERNET AND TELEPHONE VOTING FACILITIES WILL BE AVAILABLE UNTIL 5:00 P.M. E.S.T. ON THURSDAY, MAY 6, 2004.

DETACH PROXY CARD HERE IF YOU ARE NOT VOTING BY THE INTERNET OR TELEPHONE.

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acknowledged of Notice of Annual Meeting, Proxy Statement and the 2003 Annual Report.

Date            Shareholder sign here

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Date            Co-Owner sign here

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[A street map showing the location of the Annual Shareholders' Meeting is set forth in this area.]

Marriott University Park Hotel  
880 East Second Street  
Tucson, AZ 85719

520.792.4100    Hotel Direct  
800.228.9290    Reservations

TRANSPORTATION  
From Tucson International Airport

Shuttle Service  
Arizona Stagecoach  
Call 520-889-1000

Automobile - Interstate 10 to  
Speedway exit

DEAR SHAREHOLDERS:

If you previously elected to view the UniSource Energy Corporation Proxy Statements and Annual Reports over the Internet instead of receiving copies in the mail, you can now access the Proxy Statement for the 2004 Annual Shareholders' Meeting and the 2003 Annual Report on the Internet through the following address: <http://www.UniSourceEnergy.com>. You can vote your shares by telephone, the Internet, Mail or in Person at the Annual Shareholders' Meeting. See the Proxy Statement and the enclosed proxy card for further information about voting procedures.

If you would like a paper copy of the Proxy Statement and Annual Report, UniSource Energy will provide a copy to you upon request. To obtain a copy of these documents, please call 866-275-4867.

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(FORM OF PROXY CARD - BACK)

UNISOURCE ENERGY

This Proxy is Solicited on Behalf of the Board of Directors of the Company for the Annual Shareholders' Meeting to be held Friday, May 7, 2004.

P R O X Y

The undersigned hereby appoints James S. Pignatelli and Kevin P. Larson, and each of them, with the power of substitution, to represent and to vote on behalf of the undersigned all shares of Common Stock which the undersigned is entitled to vote at the Annual Shareholders' Meeting scheduled to be held at the Marriott University Park Hotel, 880 East Second Street, Tucson, Arizona, on Friday, May 7, 2004, and at any adjournments or postponements thereof, with all powers the undersigned would possess if personally present and in their discretion, upon such other business as may properly come before the meeting. This proxy, when properly executed, will be voted in the manner directed herein by the undersigned shareholder. IF NO DIRECTION IS MADE, THIS PROXY WILL BE VOTED "FOR" Proposal 1.

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