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BEFORE THE ARIZONA CORPORATION COMMISSION

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7  
8 IN THE MATTER OF THE APPLICATION  
9 OF ARIZONA PUBLIC SERVICE  
10 COMPANY FOR A HEARING TO  
11 DETERMINE THE FAIR VALUE OF THE  
12 UTILITY PROPERTY OF THE COMPANY  
13 FOR RATEMAKING PURPOSES, TO FIX  
14 A JUST AND REASONABLE RATE OF  
15 RETURN THEREON, TO APPROVE RATE  
16 SCHEDULES DESIGNED TO DEVELOP  
17 SUCH RETURN, AND FOR APPROVAL  
18 OF PURCHASED POWER CONTRACT.

Docket No. E-01345A-03-0437

Arizona Corporation Commission  
**DOCKETED**

MAR 30 2004

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**NOTICE OF FILING**

15 The Residential Utility Consumer Office ("RUCO") hereby provides notice of filing  
16 the Cross Rebuttal Testimonies of Marylee Diaz Cortez and Dr. John Stutz in the above-  
17 referenced matter.

18 RESPECTFULLY SUBMITTED this 30<sup>th</sup> day of March, 2004.

19  
20   
21 Scott S. Wakefield  
22 Chief Counsel

1 AN ORIGINAL AND THIRTEEN COPIES  
2 of the foregoing filed this 30<sup>th</sup> day  
3 of March, 2004 with:

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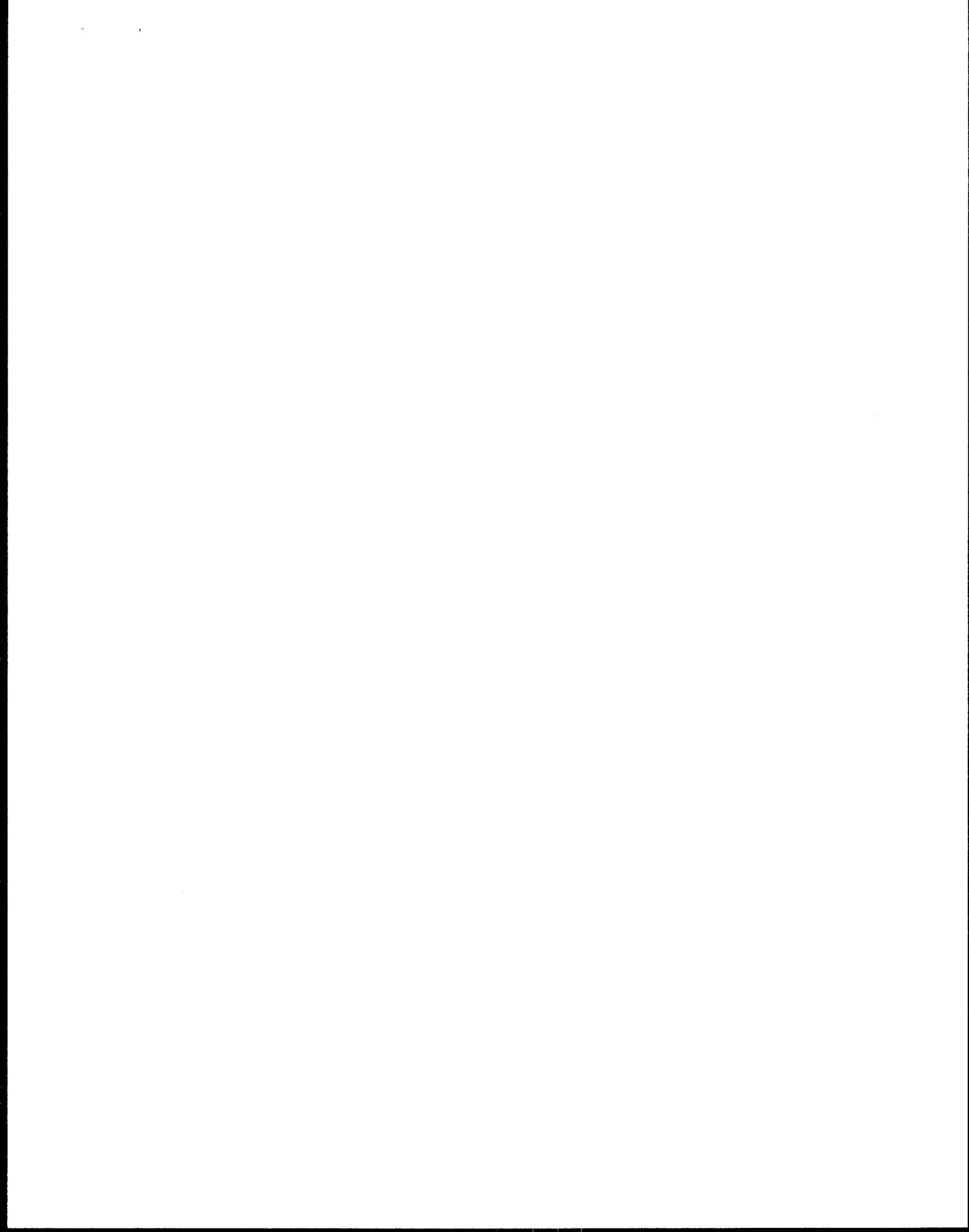
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By   
Jennifer Rumph



**ARIZONA PUBLIC SERVICE COMPANY**

**DOCKET NO. E-01345A-03-0437**

**CROSS REBUTTAL TESTIMONY**

**OF**

**MARYLEE DIAZ CORTEZ**

**ON BEHALF OF**

**THE**

**RESIDENTIAL UTILITY CONSUMER OFFICE**

**MARCH 30, 2004**

1 **INTRODUCTION**

2

3 Q. Please state your name.

4 A. My name is Marylee Diaz Cortez.

5

6 Q. Have you previously filed testimony in this docket?

7 A. Yes. I filed direct testimony in this docket on February 3, 2004 on behalf  
8 of the Residential Utility Consumer Office.

9

10 Q. What is the purpose of your cross rebuttal testimony?

11 A. The purpose of my cross rebuttal testimony is to respond to the positions  
12 taken by parties other than APS in their direct testimonies. Later, when I  
13 file surrebuttal testimony, I will address APS' rebuttal positions. Given the  
14 number of other parties in this docket and the respective number of  
15 witnesses that have filed direct testimony, my cross rebuttal will not  
16 respond to each and every position taken. Thus, the absence of cross  
17 rebuttal on any given witness or position should not be construed to mean  
18 agreement with that position.

19

20 **DEMAND-SIDE MANAGEMENT**

21 Q. Have you reviewed the testimony of Staff witness Barbara Keene  
22 regarding demand side management?

23 A. Yes.

24

1 Q. Do you agree with Staff's position regarding demand side management?

2 A. No. First, while Staff, in general, supports the use of demand side  
3 management to meet load growth, it has not proposed a specific level of  
4 funding. Second, RUCO does not agree with Staff's proposed method of  
5 funding APS's demand side management programs.

6  
7 Q. Please discuss your first objection to the Staff's position on demand side  
8 management.

9 A. The Staff has not proposed a specific level of funding for DSM programs.  
10 While the Staff supports the continuation of existing demand side  
11 management programs, it recommends that funding should be capped at  
12 \$4 million a year, which is even less than \$6 million than is currently  
13 embedded in rates. RUCO believes that Arizona should take an  
14 aggressive approach to DSM, and, that to do so, adequate levels of  
15 funding are necessary. The use of DSM to address load growth is  
16 desirable because it is beneficial to all affected parties. It allows the  
17 Company to grow and increase its customer base, without the need for  
18 long expensive power plant construction projects. This lowers stockholder  
19 risk, mitigates upward pressure such construction projects would have on  
20 electric rates, as well as detrimental effects the operation of additional  
21 generation would have on the environment. Ratepayers can also benefit  
22 from DSM programs through their ability to control and/or cut consumption  
23 and thereby lower their energy bills. There is much to be gained from an

1 aggressive approach to demand side management. However, if not  
2 adequately funded, these benefits cannot be realized. The Staff's  
3 recommended level of funding is simply not sufficient to realize any  
4 meaningful results.

5

6 Q. Please discuss your second objection to the Staff's DSM  
7 recommendations.

8 A. The Staff recommends that the DSM programs be funded through an  
9 adjustment mechanism. This adjustment mechanism would be an  
10 additional charge per Kwh consumed, and would appear as a separate  
11 item on customer bills.

12

13 Q. Why is the Staff recommending that DSM be funded through an adjustor  
14 mechanism?

15 A. Staff claims the use of an adjustor mechanism to recover DSM costs is  
16 desirable because it would allow APS the flexibility to adjust funding levels  
17 as necessary and provide incentives for APS to initiate programs at any  
18 time, rather than just in rate cases.

19

20 Q. Do you agree with the Staff's recommendation?

21 A. No. RUCO supports the recovery of its recommended level of DSM  
22 through base rates.

23

1 Q. What are the reasons behind your recommendation?

2 A. RUCO recommends base rate recovery of DSM for the following reasons:

3 1) Separately identified surcharges on bills can mistakenly be  
4 perceived to be additional taxes by customers;

5 2) The DSM expenses will be a fixed amount under RUCO's  
6 proposal (\$35 million) and thus, does not meet the criteria of  
7 volatile and widely fluctuating for automatic adjustment;

8 3) Base rate treatment coupled with a balancing account  
9 insures that APS will expend the allotted funds on DSM or  
10 will be required to refund the difference directly to ratepayer.

11

12 Q. Will RUCO's recommended DSM funding method also achieve the  
13 objectives cited by Staff?

14 A. Yes. RUCO's proposed funding through base rates will allow APS 100%  
15 recovery of all DSM expenditures up to \$35 million and allows APS  
16 flexibility to initiate new programs at any time, the two objectives cited by  
17 Staff.

18

19 Q. Please summarize your objections to the Staff DSM recommendation.

20 A. First, the \$4 million in funding is not sufficient to achieve any meaningful  
21 change in APS load. Second, DSM expenditures do not meet the criteria  
22 for automatic adjustment mechanisms. Further, the appearance of  
23 additional line item charges on utility bills unduly raises customer

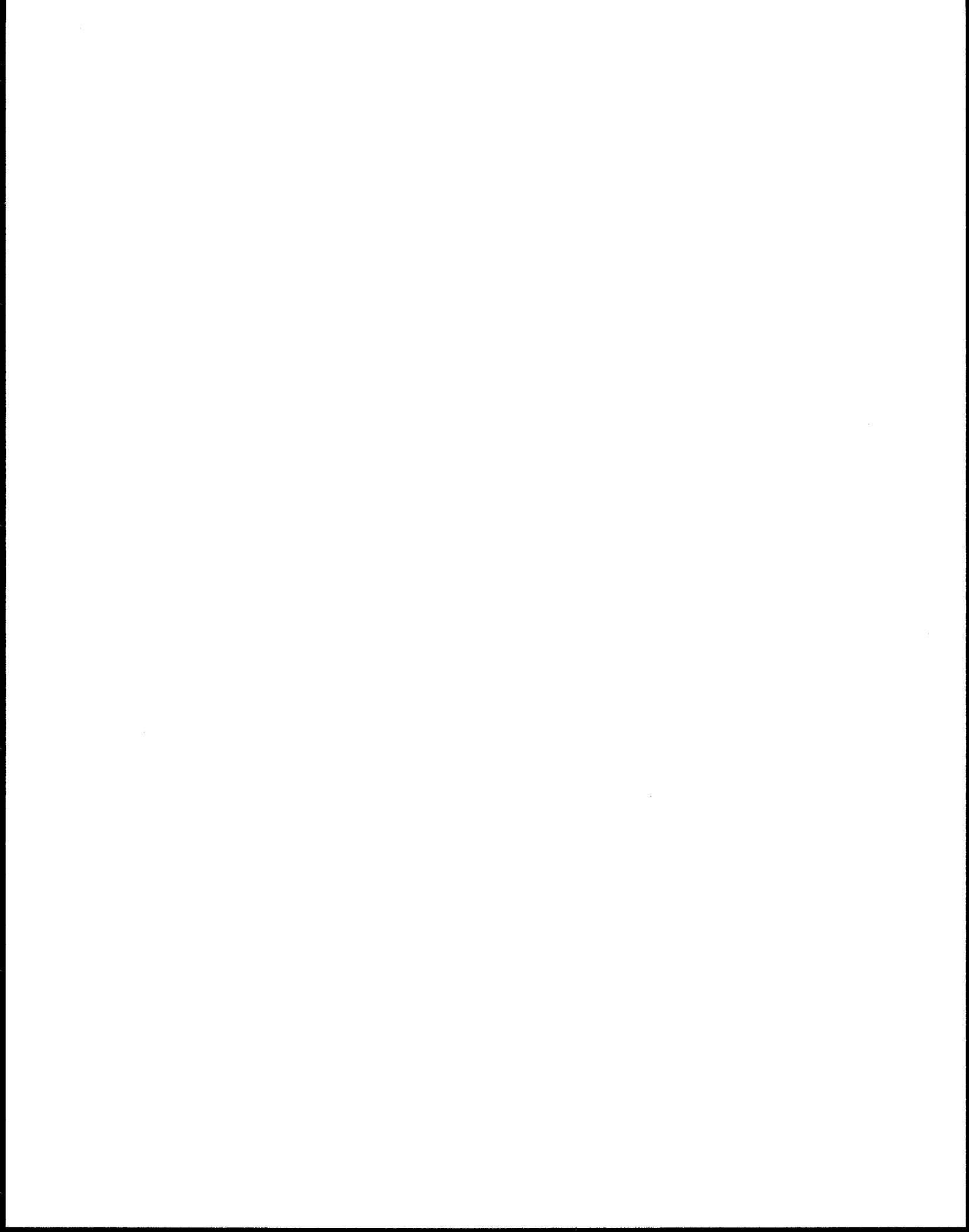
1 concerns, particularly concerns of additional taxation. RUCO believes its  
2 recommended approach to DSM and DSM funding will promote good  
3 programs with meaningful results.

4

5 Q. Does this conclude your cross rebuttal testimony?

6 A. Yes.

7



**BEFORE THE ARIZONA CORPORATION COMMISSION**

IN THE MATTER OF THE APPLICATION OF )  
ARIZONA PUBLIC SERVICE COMPANY FOR )  
HEARING TO DETERMINE THE FAIR VALUE OF )  
THE UTILITY PROPERTY OF THE COMPANY FOR )  
RATEMAKING PURPOSES, TO FIX A JUST AND )  
REASONABLE RATE OF RETURN THEREON, TO )  
APPROVE RATE SCHEDULES DESIGNED TO )  
DEVELOP SUCH RETURN, AND FOR APPROVAL )  
OF PURCHASED POWER CONTRACT )

Docket No. E-A  
01345A-03-0437

**CROSS REBUTTAL**

**OF**

**DR. JOHN STUTZ**

**On Behalf of the Arizona  
Residential Utility Consumer Office**

**Tellus Institute  
11 Arlington Street  
Boston, MA 02116-3411  
Tel: 617/266-5400**

**March 30, 2004**

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Schedule JS-14      Recommended Revenue Spreads

1 **1. SUMMARY AND RECOMMENDATIONS**

2

3 **Q. PLEASE STATE YOUR NAME AND ADDRESS.**

4 A My name is John K. Stutz. My business address is the Tellus Institute (Tellus), 11  
5 Arlington Street, Boston, Massachusetts 02116-3411.

6

7 **Q. DID YOU FILE DIRECT TESTIMONY IN THIS PROCEEDING?**

8 A. Yes, I did.

9

10 **Q. WHAT IS THE PURPOSE OF YOUR CROSS REBUTTAL TESTIMONY?**

11 A. My testimony responds to the testimony of Ms. Lee Smith, Ms. Erinn Andreasen, and  
12 Ms. Barbara Keene on behalf of ACC Staff, and to the testimony of Mr. Steven  
13 Baron, Mr. Dennis Goins, and Mr. Kevin Higgins on behalf of various intervenors.  
14 (In what follows I will refer to Messrs. Baron, Goins and Higgins jointly as “the  
15 Intervenors”),

16

17 **Q. WHAT ARE THE KEY POINTS OF YOUR CROSS REBUTTAL?**

18 A. My key points are presented below. For convenience they are grouped to correspond  
19 to the sections of my detailed testimony.

20 **COSS Development**

- 21 • Generation-related costs should be allocated on the basis of  
22 demand and energy.

- 1                   • The Peak and Average allocator should weight the average component  
2                   based on APS' investment in generating plant, not the system load factor.

3                   **Revenue Spread**

- 4                   • In developing their recommendations, the Intervenors rely  
5                   inappropriately on COSS developed using the 4CP allocator.  
6                   • The recommendations of Staff and the Intervenors lack  
7                   Bonbright's practical attributes of understandability and public  
8                   acceptability.

9                   **Other Changes**

- 10                  • Elimination of rates E-10 and EC-1 is both unnecessary and  
11                  contrary to the principle of rate stability.  
12                  • Staff's proposal to add a new charge and to increase existing  
13                  charges by up to 100 percent is inconsistent with rate stability, and  
14                  fails to spread burdens equitably.

15  
16                  **Q.     WHAT ARE YOUR RECOMMENDATIONS?**

17                  A.     In addition to the seven recommendations presented in my direct testimony, I  
18                  recommend that the Commission reject APS' use of the 4CP method in favor of the  
19                  Peak and Average method recommended by Staff. However, Staff's weighting of the  
20                  average component should be modified as described in my testimony.



1 testimony does not address, and indeed does not even mention, the fact—supported  
2 by the APS’ own witnesses, Mr. Bhatti and Mr. Wheeler—that plant was built to both  
3 meet peak and lower energy costs. Staff, on the other hand, recognizes and discusses  
4 this point. Staff recommends, as I do, that the 4CP allocation method be rejected and  
5 instead that generation-related costs be allocated on the basis of energy and demand.  
6

7 **Q. PLEASE DISCUSS STAFF’S PROPOSED ALLOCATOR FOR**  
8 **GENERATION-RELATED COSTS.**

9 A. Staff proposes the use of the Peak and Average allocation method. I support the use  
10 of this method, and have recommended its use by APS in the past. However, I differ  
11 with Staff’s construction of the Peak and Average allocator. Staff recommends that  
12 the average (i.e., energy) component of the allocator be given a weight equal to the  
13 coincident load factor. Instead, I would recommend applying the Equivalent Peaker  
14 method. That method divides the cost of the Company’s generating plant into the cost  
15 of an equivalent amount of peaking capacity, classified as demand-related, and a  
16 residual cost classified as energy-related. The peak and average components are  
17 weighted in the same proportion as the demand and energy components of the plant  
18 cost.  
19

20 **Q. IS THIS WEIGHTING CONSISTENT WITH STAFF’S ARGUMENTS FOR**  
21 **THE ADOPTION OF THE PEAK AND AVERAGE METHOD?**

22 A. Yes. The NARUC Manual describes the Equivalent Peaker method as follows:

1 Equivalent peaker methods are based on generation expansion  
2 planning practices, which consider peak demand loads and energy  
3 loads separately in determining the need for additional generating  
4 capacity and the most cost-effective type of capacity to be added.

5 (NARUC Manual, page 52, emphasis in original)

6 Use of the Equivalent Peaker method ensures that the weighting in the Peak and  
7 Average allocator will correctly reflect the amount and type of plant APS has built.  
8 The importance of both the amount and type of plant constructed is what Staff  
9 emphasized in its argument for the use of the Peak and Average allocation method.

10

11 **Q. WOULD YOUR WEIGHTING SIGNIFICANTLY AFFECT THE**  
12 **CONSTRUCTION OF THE PEAK AND AVERAGE ALLOCATOR?**

13 A. Yes, likely it would. Use of the load factor gives the average component a weight of  
14 56 percent. The analysis discussed in my 1991 testimony in an APS retail rate case  
15 (Docket No. U-1345-90-007) showed that the Equivalent Peaker produces a  
16 weighting of 80 percent or more for the average component.

17

1 **3. REVENUE SPREAD**

2

3 **Q. WHAT IS REVENUE SPREAD?**

4 A. Revenue spread refers to the pattern of increases or decreases in revenue requirements  
5 that the Commission might approve. Staff and the Intervenors have all made  
6 proposals concerning revenue spread. Schedule JS-14 provides a brief summary of  
7 these proposals for APS' two major customer classes, Residential and General  
8 Service.

9

10 **Q. DO YOU HAVE ANY COMMENTS ON THE DEVELOPMENT OF THE**  
11 **STAFF AND INTERVENORS REVENUE SPREAD PROPOSALS?**

12 A. Yes, I do. All of the Intervenors base their proposals, in part, on COSS results  
13 developed using the 4CP allocator. As I explained in my direct testimony and in the  
14 preceding section, use of this allocator is inappropriate. The Intervenors also  
15 characterize revenue requirements that produce class rates of return less than the  
16 Company average, resulting in a subsidy. Correctly used, the term "subsidy" refers to  
17 pricing below marginal not embedded cost as the interveners appear to assume.  
18 Rather than completely removing "subsidies," as the Intervenors' analyses suggest, a  
19 reasonable goal for COSS is to gradually move class rates of return toward unity.

20

21 Staff's revenue spread is based on a more appropriate COSS than that relied upon by  
22 the Intervenors. However, as I explained in the preceding section, there are still  
23 problems with the construction of Staff's Peak and Average allocator. Further, as I

1 noted in my direct testimony, there is the anomalous effect of APS' treatment of  
2 transmission on COSS results to consider. Taking all of this into account, in my view  
3 none of the COSS results currently available provide a reasonable basis for a  
4 departure from across-the-board increases or decreases.

5  
6 **Q. PLEASE DISCUSS THE ROLE OF JUDGMENT IN STAFF AND**  
7 **INTERVENORS REVENUE SPREAD PROPOSALS.**

8 A. While all of the proposals rely on COSS for support, all are based substantially on  
9 judgment. With this in mind, I would ask the Commissioners to look carefully at the  
10 numbers in Schedule JS-14 and ask themselves the following questions:

- 11 • The vast majority of APS customers are residential. Is it reasonable  
12 to give these customers 36 to 50 percent more than the average  
13 increase, or less than half of the average decrease?  
14 • Are such disproportionate allocations likely to satisfy the practical  
15 requirements of understanding and public acceptance contained in  
16 Bonbright's well-known *Criteria of a Sound Rate Structure*  
17 (Bonbright's criteria are reproduced in my Schedule JS-8).

18 In my view, the answer to both of these questions is "no."  
19

20 **Q. DO YOU HAVE ANY COMMENTS ON STAFF'S REVENUE SPREAD**  
21 **PROPOSAL?**

22 A. Yes, I do. Staff has proposed unspecified differences in the decreases for individual  
23 rates. For the reasons discussed in my direct testimony, such differences are

1 inappropriate. I recommend that any decrease (or increase) be applied across-the-  
2 board to all residential rates.

3

1  
2  
3 **4. OTHER CHANGES**

4 **Q. WHAT ISSUES WILL YOU ADDRESS IN THIS SECTION?**

5 A. I will address two issues raised in Staff's testimony: eliminating rates E-10 and EC-1  
6 and changing service charges substantially.

7 **Q. DO YOU SUPPORT THE PROPOSED ELIMINATION OF E-10 AND EC-1?**

8 A. No. There is a strong presumption in electric utility ratemaking in favor of existing  
9 rates. Bonbright expresses this presumption, in his *Criteria of a Sound Rate Structure*,  
10 through the maxim "The best tax is an old tax." Eliminating rates E-10 and EC-1  
11 would affect about 120,000 of APS' customers. Staff has identified no specific need  
12 to eliminate these rates now. Nor has it identified any benefit of immediate  
13 elimination. As Staff noted, when these two rates were closed 67 percent of  
14 residential customers were on them. Now the figure is about 15. Keeping things as  
15 they are will allow the rates to be eliminated by the gradual departure, rather than by  
16 an abrupt, disruptive change.

17  
18 **Q. PLEASE DISCUSS STAFF'S PROPOSAL TO CHANGE SERVICE**  
19 **CHARGES.**

20 A. In conjunction with a recommended decrease of 8.1 percent, Staff has recommended  
21 the addition of a new service charge as well as increases in existing charges ranging  
22 up to 100 percent. From the response to Q.1.9 from RUCO to Staff, it appears that  
23 Staff's recommendations are meant to track increases in costs. Cost tracking does not

1 give weight to the avoidance of unanticipated adverse impacts, as called for in  
2 Bonbright's Criterion of Rate Stability. Further, the addition of a new charge and  
3 increases of up to 100 percent fail to address the concern for equitable treatment of all  
4 customers that Staff displayed in developing its recommended revenue spread.

5

6 **Q. ARE YOU OPPOSED TO ANY INCREASE IN SERVICE CHARGES?**

7 A. No. The increase in costs does need to be conveyed via a price signal. However, in  
8 the face of a recommended decrease, the 15 percent cap on increases in existing  
9 charges and rejection of a new charge, is appropriate.

10

11 **Q. DOES THIS CONCLUDE YOUR CROSS REBUTTAL?**

12 A. Yes, it does.

**RECOMMENDED REVENUE SPREADS**  
**(Percent of Average Change)**

Witness	Residential		General Service	
	Increase	Decrease	Increase	Decrease
Propper	100	NA	100	NA
Andreasen	NA	49	NA	162
Baron	136	NA	61	NA
Goins	150	NA	49	NA
Higgins	138	NA	60	125
Stutz	100	100	100	100