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BEFORE THE ARIZONA CORPORATION COMMISSION

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IN THE MATTER OF THE GENERIC PROCEEDINGS CONCERNING ELECTRIC RESTRUCTURING	DOCKET NO. E-00000A-02-0051
IN THE MATTER OF ARIZONA PUBLIC SERVICE COMPANY'S REQUEST FOR VARIANCE OF CERTAIN REQUIREMENTS OF A.A.C. R14-2-1606	DOCKET NO. E-01345A-01-0822
IN THE MATTER OF THE GENERIC PROCEEDING CONCERNING THE ARIZONA INDEPENDENT SCHEDULING ADMINISTRATOR	DOCKET NO. E-00000A-01-0630
ISSUES IN THE MATTER OF TUCSON ELECTRIC POWER COMPANY'S APPLICATION FOR A VARIANCE OF CERTAIN ELECTRIC COMPETITION RULES COMPLIANCE DATES.	DOCKET NO. E-01933A-02-0069

EXCEPTIONS OF ARIZONA PUBLIC SERVICE COMPANY TO THE RECOMMENDED OPINION AND ORDER ON "TRACK B" ISSUES

Pursuant to A.A.C. R14-3-110(B), Arizona Public Service Company ("APS" or "Company") submits these Exceptions to the Recommended Opinion and Order on Track B issues ("Recommended Order") issued by the assigned Administrative Law Judge ("ALJ") on January 29, 2002.[1] The Company's Exceptions also will address, where necessary, the ALJ's proposed amendment of February 4, 2003 ("ALJ Amendment") to her Recommended Order.

[1] In addition to the arguments specifically set forth below, APS incorporates by reference the arguments made in its post-hearing briefs filed on December 18, 2002 and December 31, 2002.

I.
INTRODUCTION

APS is and has been willing to competitively solicit power for the benefit of its customers.[2] It actively participated in every workshop, responded to literally hundreds of data requests, voluntarily provided Staff and its facilitator with information they requested, and has worked diligently to implement the Staff-proposed process even though there was no Commission order adopting or mandating that process. In that respect, APS is working closely with Staff's recently selected independent monitor. The Company's goal is to work with the Commission and the independent monitor to facilitate a timely Track B procurement. APS has also complied in a timely fashion with every Track A requirement, including the filing last fall of its expanded Code of Conduct and the completion of a Reliability Must-Run ("RMR") study for both metro-Phoenix and Yuma. APS has also restructured and reorganized its procurement organization to satisfy Staff and merchant concerns.

The Track B proceeding itself presented the ALJ with many regulatory issues new to Arizona, and in some instances, unprecedented in the United States, and thus there was little or no authority to which she could look. There also were many parties taking diverse positions on virtually every one of these issues. Indeed, the goals themselves of Track B were often inconsistent and sometimes impossible to reconcile, and APS does not envy the ALJ's task in this matter. But although the Company acknowledges the hard work of the ALJ in conducting an eminently fair hearing and drafting a comprehensive

[2] The Recommended Order is incorrect in stating that "APS had chosen not to commence the competitive bid that rule [1606] required, but instead [proposed the variance.]" (Recommended Order at 63.) First of all, there was no such requirement for APS to "commence" in 2001, since the requirement had been postponed by order of the Commission until January 1, 2003. *See* Decision No. 61973 (October 6, 1999). Moreover in its April 2002 Motion for Threshold Determination, APS wrote "If the Request for Partial Variance is denied or is not decided by September 1, 2002, APS will issue an RFP or RFPs for at least the full 50 percent requirement specified in Rule 1606(B)." (Emphasis added.) APS never contended that the Commission could not reach a different conclusion and never refused or threatened to refuse to implement Rule 1606(B).

Recommended Order, APS must take strong exception to many parts of that Recommended Order and will propose a number of substantive amendments to such Recommended Order.

Throughout the Track B process, there has been at least one theme upon which all parties expressed agreement—that the end result should benefit customers in Arizona. However, the Recommended Order as drafted will not benefit customers. If not substantially modified, it has a very real prospect of causing higher costs for APS customers that could take years to undo. The Recommended Order's overly-rigid, and now time-constrained, procurement process ignores the proven (and unquestioned) procurement and risk management practices that APS has successfully used to weather the storm in wholesale power markets over the last several years. During the same period, utility customers in most other western states endured double-digit rate increases and once highly rated utility companies collapsed under the burden of a well-intentioned but ultimately flawed experiment. Most troubling, the Recommended Order appears to toss aside what APS believed was a cornerstone of the Commission's decision to reverse the divestiture requirement in the Track A order, Decision No. 65154 (September 10, 2002)—that the public interest required a more prudent and cautious transition toward retail electric competition using utility-owned generation as the essential "hedge" for such gradual transition. *See* Decision No. 65154 at 23.

Instead of a measured transition to greater reliance on the wholesale market to serve the retail customer needs of APS, the Recommended Order mandates a competitive procurement that in one fell swoop significantly "straightjackets" APS' procurement and would include:

- Large-scale bidding of economy energy requirements years in advance of when anticipated, thus reducing the ability of APS to exercise the very nimbleness in securing economy energy in response to a constantly

changing marketplace that is necessary to save money for APS customers without sacrificing reliability[3];

- An apparent requirement that APS must acquire its unmet needs in the initial March 2003 Track B solicitation irrespective of price or customer impact;
- Bidding of RMR requirements already met by utility generation that APS was required to retain, in the same solicitation as other requirements, and again in a manner untested anywhere in the country;
- A solicitation that apparently must simultaneously compare not just price, stability and reliability—the long-used resource selection criteria embodied in the Commission's own resource planning regulations—but also unspecified environmental and wholesale market impact criteria with absolutely no guidance as to how to weigh or consider any of these new factors, either in conjunction with each other or against the traditional criteria;
- A period of only a few weeks for APS to review and properly select winning bids which—while perhaps achievable when only traditional evaluation of conforming bids was required—is now impractical, if not impossible, given the evaluative standards set forth in the Recommended Order and the open invitation given by such Recommended Order for the submission of non-conforming bids;
- No concurrent approval by the Commission that could validate whether or not APS has correctly navigated the maze of new and vague procurement objectives, nor any express assurance of cost-recovery even if it has should

[3] By its nature, economy energy is purchased on short notice, and the Company usually provides the operating reserves for such a purchase.

the Track B procurement otherwise result in costs *substantially higher than* APS could have achieved by continuing with its already proven, but now forbidden, procurement process; and

- *Ad hoc* standards of conduct that ignore both Staff's recommendation and the existing structure of APS and Pinnacle West Capital Corporation ("PWCC")—a structure that evolved largely in response to the Commission's prior electric competition policy—and which appear to limit necessary and reasonable oversight by officers and directors, and restrict APS' ability to access needed expertise.

APS has supported and continues to support a reasonable, appropriately phased-in transition to increased reliance on the wholesale market in Arizona. Such a reasonable process would allow for both the utilities and the Commission to develop experience and test in the real world the type of competitive procurement processes that the Commission desires to adopt. It could address the cost-effective construction or acquisition of new generation resources, and consider environmental costs in an explicit and objective manner. However, the Recommended Order's attempt to mandate a specific and inflexible structure in this very first attempt at a one-shot state-wide solicitation will neither reduce costs nor result in improvements to the environment. Neither will it benefit the wholesale market, although it will likely benefit sellers in Track B. Indeed, there is no evidence in the record that the procurement process required by the Recommended Order is or will be any better than the procurement process used today or will achieve the goal of benefiting our customers. Accordingly, APS urges the Commission to modify the Recommended Order in accordance with APS' proposed amendments, which are attached as Exhibit A and grouped by subject area.

II.
THE STANDARDS FOR EVALUATING BIDS IN THE RECOMMENDED ORDER ARE UNREASONABLY VAGUE AND IMPOSSIBLE TO SATISFY

The Recommended Order directs that:

> if APS and TEP determine, after serious economic and technical analysis of all bids, including long-term and short-term bids, that the offered capacity or energy would serve their customers more economically than their existing assets, then APS and TEP shall make procurements accordingly, keeping in mind that the goal of the competitive solicitation is to provide ratepayers reliable power at the lowest cost, while considering the environmental effects of their procurement decisions and whether their decisions further the Commission's goals of encouraging the development of a robust wholesale generation market.

(Recommended Order at 68-69, Finding of Fact No. 31 [emphasis added].)[4] The Recommended Order requires APS to engage in an impossible balancing of often mutually-exclusive objectives with absolutely no guidance—either to APS or to potential bidders—on how those objectives are to be measured and weighed against each other.

Specifically, APS is first directed to provide customers with "reliable power" at the "lowest cost," considering both long-term and short-term bids.[5] (*Id.*) In addition to procuring the "lowest cost" power, the Recommended Order directs APS to factor in

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[4] The Recommended Order states: "We disagree with APS' argument that the Track B solicitation process restricts the manner by which APS procures power." (Recommended Order at 63.) As this finding of fact plainly shows, that statement is incorrect. The Commission cannot reasonably or lawfully mandate that APS and its customers be the subjects of an experiment in wholesale electric competition that provides no regulatory validation for the outcome of that process.

[5] While this portion of the Recommended Order's multi-faceted evaluation standards may superficially appear straightforward, there are significant complicating issues to even evaluating bids solely on current price and physical reliability. These issues include counter-party credit risk, the potential for changing future market conditions resulting from federal Standard Market Design ("SMD") and Regional Transmission Organizations ("RTOs"), future retail customer attrition to Direct Access, and other market-related issues affecting price stability and predictability. For example, APS could receive a relatively low-priced bid for a 20-year contract with firm transmission delivery rights. But the risk of the counter-party defaulting in, for example, the fifth year of the contract could leave APS and its customers unreasonably exposed in any effort to cover that defaulted contract position. Similarly, an RTO may offer access to better, more economical resources for APS in the near future. The contract offer may also contain price escalation, early termination rights or other provisions that make future prices under the proposed agreement perilously uncertain. Ultimately, a 20-year contract today may not be as valuable to APS as a similar 4-year contract even if price terms are similar or even lower.

environmental effects but provides no guidance on how this is to be accomplished. How is the multitude of different potential environmental impacts to be weighed against each other? Are air emissions or water consumption more important? Are land use issues relevant, and how are they related to air emissions and water consumption? How is APS to weigh a plant that uses groundwater from a small aquifer, versus a plant using groundwater from an abundant aquifer, versus a plant using surface water, versus a plant using treated effluent? How does APS weigh higher air emissions in a sparsely-populated, rural area of the state against lower air emissions concentrated in or near a non-attainment area and dense population center? Do in-state environmental effects weigh more heavily than out-of-state impacts? And how would the analysis be applied when the potential seller does not specify any particular power plant, but rather is only delivering non-unit-contingent power to a regional market hub? How is APS to consider the fact that a potential seller's generating units will be dispatched and sell into the wholesale market regardless of the outcome of the Track B procurement? Is the only time that environmental impacts come into consideration when the costs are "comparable" to or the same as the cost of other bidders in Track B? (*See* Recommended Order at 15.) Even if this narrower evaluative standard were the case, how is fuel diversity—which affects the "reliability" requirement in the Recommended Order and the price stability or uncertainty considerations under traditional resource acquisition principles—then considered and weighed, and what does "comparable" mean?

These issues and the resulting costs and benefits under traditional regulation were evaluated in integrated resource planning ("IRP") proceedings, which often lasted for years, were contentious, and ultimately never yielded a workable method for actually quantifying any of the various environmental factors discussed above. The Recommended Order rejects RUCO's and the LAW Fund's recommendation for new IRP proceedings, deferring instead to a future workshop "to [examine] the possible costs and benefits of the

respective [demand side management and environmental risk mitigation] policies." (*Id.* at 48.) Moreover, the Recommended Order actually rejects requiring that any specific environmental information be evaluated or produced as part of the competitive solicitation, noting that:

> [T]he duties of the utilities, the Staff and the Independent Evaluator will be very time-consuming in this initial solicitation, and we do not believe that the extra burden that the recommended requirement would place on the process would yield results justifying the burden.

(*Id.* at 49.) As this workshop will occur after APS has conducted the solicitation, it will be impossible for APS to anticipate the results, and it would be unlawful and unreasonable for the Commission to require APS to portend the appropriate outcome when conducting this solicitation.

In addition to "keeping in mind" environmental effects when conducting the competitive solicitation, the Recommended Order introduces yet further ambiguity by requiring APS to somehow factor in how the solicitation will affect the development of the wholesale competitive market for generation. (*Id.* at 69.) As a practical matter, nothing APS does in the Track B solicitation will materially affect the wholesale generation market.[6] Regardless, the Recommended Order appears to adopt some sort of preference program for merchant power plants. (*Id.*) Are APS and its customers expected to pay a higher price for some merchant generator's power if doing so would help support that merchant generator? Is APS required to allocate awarded bids under a quota system so that some amount is awarded to as many merchant generators as possible? Are APS and its customers required to absorb the risk and cost impacts if a long-term contract would benefit a merchant generator but would not benefit APS? What are the metrics by which

[6] Based on the September 2002 Western Electricity Coordinating Council ("WECC") 10-Year Coordinated Plan Summary, which is a public record, the WECC has more than 169,000 MW of capacity compared to the roughly 2,500 MW of APS capacity at issue in Staff's Contestable Load Estimate. Contestable energy would be only approximately 0.5% of the WECC's annual energy requirements, even after including APS' economy energy purchases and RMR needs.

APS is to determine a "robust wholesale market?" Is it number of participants? Is it number of megawatts? Is it some measure of market liquidity? It is when the market produces prices below some threshold? Even if APS were provided with the Recommended Order's vision of what constitutes a "robust wholesale market," how would the effects on such a vision be quantified so that they could be evaluated along with the price and reliability aspects in various parties' bids?

The conflicting standards set forth in the Recommended Order, which were never discussed at any length or in any detail in the Track B hearings or workshops and were not specifically recommended by Staff, also have never been previously used in Arizona. To APS' knowledge, no other jurisdiction in the United States has proposed, much less mandated, procurement standards similar to those proposed in the Recommended Order. As written, the Recommended Order thus adopts *ad hoc* resource planning on an impossibly accelerated timeline and without the structure or protections of a formal IRP rulemaking process. And worse for the certainty and ultimate resolution of the initial Track B solicitation, the lack of any specificity in the Recommended Order will undoubtedly give rise to endless disputes and litigation over APS' evaluation and weighting of such non-commercial terms as environmental factors and competitive market considerations.

If the Recommended Order is intended to dictate a set of criteria by which APS and TEP are to review and accept bids that differs from the currently applicable standards and practice or from those set forth in Rule 1606(B)—which is precisely what the Recommended Order appears to do by requiring an unarticulated weighing of contract terms, environmental impacts, and facilitation of wholesale market development—it must be promulgated through a rulemaking proceeding. *See* A.R.S. § 41-1001(17) (defining "rule" as "an agency statement of general applicability that implements, interprets or prescribes law or policy"); A.R.S. § 41-1030 (a rule is invalid unless made and approved

in substantial conformance with the Arizona Administrative Procedure Act, A.R.S. § 41-1001, *et seq.*). And, a meaningful articulation of what those evaluative criteria are and how they should be measured and applied is also required under principles of due process. An administrative agency's rules and requirements must be sufficiently specific so that "a regulated party acting in good faith would be able to identify, with ascertainable certainty, the standards with which the agency expects parties to conform." *Trinity Broadcasting v. FCC*, 211 F.3d 618, 628 (D.C. Cir. 2000) (holding FCC minority control rule unlawfully vague); *see also General Electric Co. v. EPA*, 53 F.3d 1324, 1329 (D.C. Cir. 1995) (holding that "elemental fairness compels clarity in the statements and regulations setting forth the actions with which the agency expects the public to comply"); *State v. Tacaks*, 169 Ariz. 392, 394, 819 P.2d 978, 980 (Ct. App. 1991) (legislative enactment is unconstitutionally vague when it "does not provide explicit standards for those who will apply it").

In sum, if the Recommended Order cannot or will not articulate what it means by these new evaluative criteria and how they should be measured and applied, how can APS possibly comply with them? Accordingly, the Commission should reject the vague and impossible to comply with standards discussed in the Recommended Order and, at a minimum, defer to the position taken in the Staff Report that allows the utility to develop the appropriate selection criteria based on traditional practices. If, however, the Commission desires to conduct the type of comprehensive resource planning process embodied in the Recommended Order, it should either do so after the initial solicitation or delay the initial solicitation until such standards are appropriately and lawfully developed. To this end, APS has proposed an amendment in Exhibit A that deletes reference in the Recommended Order to any standard for evaluation of Track B bids other than the best interests of APS customers.

III.
THE PROCUREMENT PROCESS PROPOSED IN THE RECOMMENDED ORDER LACKS EVIDENTIARY SUPPORT AS WRITTEN AND SHOULD BE CLARIFIED TO BETTER REFLECT THE STAFF POSITION

A. APS' Current and Proven Process for Obtaining Purchase Power Has Not Been Shown to Be Deficient

The Commission must ask to see the evidentiary proof, anecdotal or otherwise, that the various procurement strategies being touted by the parties would yield better results than APS' current procurement practices. During the hearing, no party could provide or even offered to provide such proof. Under such circumstances, the prudent course of action would be to propose procedures that mirror those currently in place to the maximum extent possible, or at the very least, procedures that would do the least damage to a flexible and robust power procurement—one that combines auctions, RFPs, bilateral negotiation, and modern electronic trading platforms. These underlying themes were, in the Company's opinion, the essence of the Staff position during the Track B hearing. The Recommended Order, however, goes far beyond the discussions and various positions expressed in the Track B proceeding and, as discussed below, appears to call into question even some key principles that had been used to justify the original Staff proposal.

B. Right to Say "No"

For example, one of the most important rationales underlying the Staff Report was the notion that no utility would be required to accept bids for any part of the initial Track B solicitation. The ALJ Amendment, however, may be read as requiring APS to accept initial Track B bids—apparently regardless of price, or for that matter, the environmental impact—for all of the its unmet physical needs, and only allows APS to reject bids as contrary to the interests of its APS customers for its potential economy energy needs and the contestable portion of its RMR generation.[7] APS understands that it is at risk from a

[7] The language in the original Recommended Order is confusing and arguably contradictory on this issue. At one point, it states that the Commission agrees with Staff and the AUIA on this point, both of whom supported APS' right to reject any and all bids regardless of whether the bid was for unmet physical

prudence standpoint if it were to reject otherwise reasonable bids (based on information available at the time of the bid) and further accepts that the independent monitor and Staff will be closely watching the Company every step of the way for evidence of real or apparent favoritism of PWEC. However, this is far different from an affirmative mandate that APS must accept in the March 2003 Track B solicitation some level of Track B bids regardless of price. In addition to putting inevitable and significant upward price pressure on bids,[8] such a requirement unreasonably interferes with APS' risk management and unquestionably limits its control over the solicitation. Without assurances of cost recovery for such a mandate, such a limitation is also both unreasonable and unlawful.

C. Secondary Procurements

Additionally, the Staff Report allowed APS to conduct short-term, real-time and emergency procurements outside of any formal Track B solicitation. The Recommended Order, however, appears to ignore this Staff recommendation. It further incorrectly characterizes economy purchases as "unplanned or unexpected needs." (Recommended Order at 31.) Economy energy is simply energy APS (or other utilities, for that matter) purchase whenever it is cheaper to buy than to use or continue to use an existing generating or purchase power resource. The seller provides no capacity, and APS continues to provide the capacity reserves for such purchase from those existing resources. This saves customers money without compromising reliability. APS fully expects to make some level of economy energy purchases under all but the most extreme situations. And if the Track B solicitation does not yield what APS believes to be

needs, unmet economy energy, or contestable RMR. (Recommended Order at 50.) In most other places, however, the Recommended Order seemingly qualifies the right to reject by emphasizing the need to actually acquire through Track B the unmet physical needs of TEP and APS. (*See, e.g., id.* at 51.) The language in the ALJ Amendment heightens this disturbing possibility. (*See* ALJ Amendment at 2, second insertion to Page 70.)

[8] If one product (in this case, APS' reliability unmet need) in a multi-product solicitation must be purchased, irrespective of price and terms, bidders will tend to overprice that element of their bid while competitively pricing the other elements so as to maximize their overall price.

reasonable bids for this energy, there will need to be secondary procurements on such energy. Even as to the estimates of unmet reliability needs, such needs could actually turn out to be greater than the amount bid through Track B as set forth in the Recommended Order. Again this will necessitate one or more secondary procurements, as the period of anticipated need becomes closer. APS believes that it should be allowed to procure this short-term capacity and energy as it has historically done using a "blind" system (either electronic or through third-party brokers), such as was described by APS witness Thomas Carlson and praised in the Recommended Order, or an RFP or bilateral agreement. If the Recommended Order is not amended to permit this, at the very least the Recommended Order should be amended to clarify that "emergency" power includes both real-time procurement, for which APS needs significant flexibility simply to keep its control area operating reliably, and emergency power resulting from actual system supply or transmission emergencies.[9]

The Recommended Order requires APS to file for Commission approval "protocols" for secondary procurements, excepting emergencies. (*Id.* at 59.) How long such approval would take and what APS is supposed to do about secondary procurement in the meantime are left unanswered. This issue did not even come up during the Track B hearing, and so APS has no guidance as to what such "protocols" should contain and by what criteria they would be evaluated by the Commission. It is also another example of how the Recommended Order would micro-manage APS procurement practices. While APS does not oppose working with Staff and the independent monitor to develop reasonable provisions to protect from the appearance of affiliate abuse, and has already implemented on a voluntary basis procedures to negate such appearance (*id.*), this

[9] In this regard, the PWEC Arizona assets will remain available to serve APS customers if so required by then existing circumstances, even though they will not be considered in determining contestable capacity and energy, nor will they affect the award of contracts in Track B. Whether these assets will continue to be dedicated to serve APS will be determined solely by the Commission in the Company's next general rate proceeding.

recommendation as proposed cannot be implemented in time for the 2003 Track B procurement. APS' proposed amendment retains the concept of secondary procurement protocols, but leaves them to be worked out by Staff and the independent monitor rather than requiring affirmative Commission approval of such protocols.

The Company is already providing Staff and then the other parties with Standards of Conduct to govern the actual Track B solicitation. The Recommended Order itself provides for a hearing this spring on the expanded Code of Conduct APS filed last fall in response to Decision No. 65154. (*Id.* at 56.) That proceeding will have the benefit of the monitor's report on Track B, as well as any observations made by Staff as to how APS has handled affiliates during that process. This is the appropriate forum to consider whether yet further restrictions need to be imposed on APS procurement policies and at what cost to APS customers.

Perhaps the broader issue here is the definition of "Track B." Is it simply the one-time procurement that is scheduled to commence in March of 2003? Does it include similar type procurements during the spring of every year? Or does it encompass any sort of secondary procurement, including real-time purchases? APS urges the Commission to await the results of this first 2003 Track B procurement before making any decisions about future "Track Bs," while permitting utilities to make secondary procurements as necessary and appropriate to best serve the interests of their customers.

D. Economy Energy

As noted earlier, economy purchases are opportunity purchases of energy without associated capacity based on known or anticipated opportunity costs. APS opposes the inclusion of economy energy in the Track B process as being impractical, unprecedented anywhere in the country, and beyond the scope of Track B as set forth in Decision No.

65154.[10] However, APS will not oppose considering bids for such energy in Track B with the continued understanding that it can decline to accept any or all such bids. APS would, of course, respond in future rate proceedings to any challenge of such a refusal to accept economy energy bids (just as it must now) and needs to justify that refusal. However, to suggest (Recommended Order at 33) that APS' acquisition of economy energy is different in any respect from that of TEP is both one hundred percent inaccurate and wholly unsupported by the record. The purchase of economy energy is no more "planned" or anticipated for APS than for TEP, but in both cases it can be roughly estimated given a specific set of assumptions. The existence of affiliated generation is not one of those assumptions, and thus was and is entirely irrelevant to this issue.[11] If the Commission is determined to change something about the acquisition of economy energy, this entire discussion in the Recommended Order should be largely deleted and substituted with a simple finding that both APS and TEP should solicit Track B bids for their estimates of such energy as a means to better test the full range of the market but have no obligation to accept any such bids.

E. RMR

The Track A Decision said nothing about and certainly does not require bidding existing utility-owned generation of any sort, let alone utility-owned RMR generation.

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[10] The Recommended Order's apparent belief that Decision No. 65154 imposed no limits on competitive procurement from the competitive market is clearly contrary to the express language in that Decision and to the Staff position in Track A, which such Decision essentially adopts. (*See* Recommended Order at 14.)

[11] Both in this discussion and in that of the Standard of Conduct provisions, the Recommended Order appears to draw some link between this proceeding and the Company's requested Partial Variance to Rule 1606(B) filed in October 2001. There is no such link. Neither is there any connection between APS' August 2002 estimate of unmet need and Decision No. 65154, as is suggested at page 31 of the Recommended Order. The August estimate was simply a set of bad numbers for reasons the Company has explained *ad nauseam*, as has been fully recognized by Staff in Exhibit S-5. And the statement that APS has changed its historic approach to purchasing economy energy (which the record indicates is clearly not a "spot market" strategy) between August and November of 2002 is both wrong and unsupported by any evidence of record.

Staff witness Matt Rowell specifically opposed such bidding in Track A. Indeed, this entire issue reflected a dramatic change in Staff's position not just from that taken in Track A, but from the time it filed its "final" report in October 2002 to the filing of its testimony in November 2002. Not surprisingly, there is nothing in the record as to how these existing units should be "bid" or how such bids should be evaluated in the very limited time allowed under the proposed Track B procurement schedule.

A generating unit is only in RMR status during those hours of the year when the load within a given area (*e.g.*, metro-Phoenix) exceeds its transmission import capability. Under such circumstances, that excess amount (and only that excess amount) of load must be served from local generation. This happens infrequently, and even when it does there is often little or no additional cost to consumers. The recent RMR study submitted by APS in conformance with the Track A order and the Biennial Transmission Assessment[12] confirms the insignificant economic and very limited environmental impact of RMR. And in the metro-Phoenix area, only APS, PWEC and SRP have local generation.[13] Since the availability of SRP generation in excess of its own native load within the metro-Phoenix area is unknown, the only dependable bidder for such demand and energy in the near term would be PWEC. Likewise, in Yuma the only non-APS entities having generation within the constraint already have contracts for their output in California. Thus, at least for the

[12] The Recommended Order incorrectly states that the 2003 RMR Study will cover the period through 2007. (*Id.* at 25.) The Biennial Transmission Assessment required the first RMR Study to cover the period from 2003 to 2005.

[13] Some of the merchant intervenors believe they can deliver power from outside the constrained area during RMR hours. Although this claim is not supported by the record, APS is willing to keep an open mind and will consider such proposals in the upcoming Track B solicitation, but not as RMR alternatives. This is because even if such claims can be demonstrated as valid, it would not mean these merchants could bid on RMR load and energy. It would instead mean that RMR conditions do not, in fact exist, because there is still available transmission into the constrained area. Thus, such potential sellers could be considered as part of the more general solicitation of what the Recommended Order terms "contestable load."

next several years, the Recommended Order's requirement that APS bid its Phoenix and Yuma RMR requirements is, at best, unnecessary.

Longer term, there is more value in analyzing RMR alternatives in a systematic and thoughtful fashion. New local generation, increased transmission import capability, and load management within the constraint should all be considered, but not in some rushed, cobbled-together procurement scheduled to begin in a few weeks. In fact, this entire issue of RMR is deserving of more than one page of analysis and discussion and should be deleted from the Commission's final order. Neither APS nor TEP realized it even was an issue until less than three months ago. Like IRP and environmental risk management, a series of workshops to follow up on the RMR studies filed in January 2003 (again in response to Decision No. 65154) is a better course than attempting to rush into place a procurement without direction and apparently, for the present, without purpose. Indeed, the Commission has already scheduled one such workshop for February 18, 2003.

F. Staggering the Track B Procurement Evaluation

Given the Recommended Order's requirement that APS and TEP entertain a wide multitude of long-term and short-term bids—bids that apparently need not offer any of the products actually needed by either APS or TEP (Recommended Order at 42)—and the need to "seriously evaluate and consider" all such non-conforming offers, APS believes it appropriate to stagger the evaluation of bids. Those bids offering conforming products for 2003 should be evaluated and awarded more or less on the schedule proposed by Staff. Bids for later years or non-conforming bids would be given an extra three weeks for evaluation and possible award. And depending on how unusual or novel a particular bid proposal was, it may also be necessary to allow yet additional time for final contract execution.

IV.
THE PROCESS IN THE RECOMMENDED ORDER FURTHER SUPPORTS THE NEED FOR COMMISSION APPROVAL OF THE SOLICITATION AND RESULTING CONTRACTS

Most of the potential participants in the competitive solicitation advocated Commission approval of the contracts and/or solicitation process to reduce uncertainty and ultimately lower costs. Staff argued that Commission approval of the outcome was too risky, essentially because the proposed procurement process was new and the Commission lacked experience with the process. The Recommended Order claims to leave the "responsibility and choice of procurement squarely in the lap of the utility" (Recommended Order at 63), but then significantly limits and restricts the ability of APS to manage procurement in a manner and on a schedule that it believes are appropriate.

Because the Recommended Order now proposes to require some unarticulated and unexplained form of balancing of cost, reliability, term, environmental effects, and wholesale market development, the Commission should either (1) provide APS specific guidance on how to implement the Commission's desires on wholesale generation procurement well before purporting to hold APS accountable for its procurement choices, or (2) review and approve the procurement choices when APS conducts the solicitation. Other states that have become active in wholesale generation competition, such as New Jersey, do not shy away from the responsibility associated with deciding to mandate a wholesale procurement process.[14] States like Nevada are approving long-term contracts from some of the same merchant generators as are likely to participate in the Track B

[14] *See, e.g.,* R.C.S.A. § 16-243a-6 (Connecticut commission reviews evaluation of generation RFPs to ensure consistency and approves results); Feb. 6, 2003 Decision, Docket No. EX01110754 (New Jersey B.P.U.) (New Jersey commission certifying statewide generation auction and approving auction results within two days); Nov. 14, 2002 Settlement Agreement, Md. P.S.C. Docket No. 8908 (Maryland commission will approve bid plans and approve results; although a commission decision is still pending, the commission Staff supports the settlement); Decision 02-12-074 (Cal. P.U.C., December 19, 2002) (approving California utilities' short-term procurement plans).

procurement.[15] This Commission has also historically pre-approved APS' long-term power contracts, including both the Pacificorp exchange and the SRP Territorial and Contingent contract. Not surprisingly, these are the only long-term agreements APS presently has in place.

The Recommended Order's prescriptive treatment of secondary procurements, as described in Section III.C., is another argument for Commission approval of any contract procured using Commission-mandated procedures. The power to micro-manage must be matched by assuming the responsibilities of such management, including the responsibility for assuring full and timely cost recovery. As tempting as it may be to employ a 20/20 hindsight standard for prudence determinations, it will neither promote "robust" wholesale competition nor be fair to utilities to have them making these important Track B decisions for years into the future without regulatory assurance that the results of this mandated process will receive supportive regulatory treatment. APS and TEP have to make real choices under already difficult and time-constrained conditions, and it is particularly unreasonable when the standards by which the procurement is to be evaluated are impermissibly vague, often mutually exclusive, and likely unattainable through Track B.

The Recommended Order's response to all these concerns is to brush them aside with first the statement that the Track B solicitation process imposed by the Recommended Order does not restrict the manner by which APS procures power. (Recommended Order at 63.) After more than 60 pages of a Recommended Order that imposes one restriction on the Company after the other, this statement has more than a hollow ring. The Recommended Order also states that any financial impact on APS is "within APS' control" because "APS will make the decision as to how much competitive power to procure." (Recommended Order at 15.) Yet the ALJ Amendment to the

[15] *See* NAC 709.939 (2) (Nevada regulations regarding power procurement).

Recommended Order arguably removes "the decision as to how much competitive power to procure" entirely from the Company's control with respect to a large component of the Track B solicitation. (ALJ Amendment at 2.)

V.
THE STANDARDS OF CONDUCT ARE TOO VAGUE AND ARE UNREASONABLY RESTRICTIVE

In every step of the electric restructuring process, APS has complied with the Commission's rules and regulations and, whenever required, has sought specific Commission pre-approval of its actions. Although certain of the merchant intervenors have argued that the Commission should implement unreasonably harsh rules to prevent the possibility that APS might favor one of its affiliates in some improper fashion, none of those parties has offered any proof that APS has circumvented the Commission's Affiliate Rules or has violated APS' Code of Conduct. Despite this, the Recommended Order goes far beyond what Staff proposed.[16] When examined in the light of reality, it is clear that the Recommended Order's proposed "guidelines" are impossible to comply with in any meaningful fashion and raise serious questions as to their potential adverse impact on corporate management's ability to meet its responsibility and accountability for corporate governance and activities.

The Recommended Order acknowledges that APS has submitted a proposed Code of Conduct in compliance with the Track A order. (Recommended Order at 56.) APS also will be submitting to Staff and the Independent Monitor proposed Standards of Conduct for the solicitation process. The merchant intervenors will be given an opportunity to comment on both the Code of Conduct and Standards of Conduct. The Recommended Order also recognizes that the Independent Monitor and Staff will be intimately involved

[16] Most of the merchant intervenors, as well as Staff have recognized (at least implicitly, if not expressly) the need to consider the PWCC corporate structure developed in response to the Commission's Electric Competition Rules.

in, and will oversee, the solicitation process with the explicit direction to watch for unfair or preferential treatment of any bidder. (*Id.*) Yet, despite all of those protections, the Recommended Order concludes that it is necessary to impose additional "guidelines" that mandate clearly unworkable, and effectively punitive, standards of conduct. The Recommended Order also interjects itself into the FERC issue of the El Paso Natural Gas transportation agreement with APS and PWEC. And in doing so, it misunderstands and misstates the issue before FERC. (*See* Recommended Order at 58.) While all of the participants in the Track B proceeding supported a transparent and fair solicitation process—a process that would be fair to all parties involved, including APS—the Recommended Order effectively ties APS' hands.

Moreover, the "guidelines" also would conflict with the spirit of the information and reporting obligations imposed by Sarbanes-Oxley. *See* Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (July 30, 2002). It also threatens the ability of Pinnacle West management to exercise their fiduciary duty to oversee activities by major subsidiary entities such as APS and PWEC. *See, e.g.,* A.R.S. § 10-830 (duties of directors); A.R.S. § 10-842 (duties of corporate officers); *AMERCO v. Shoen*, 184 Ariz. 150, 157, 907 P.2d 536, 543 (Ct. App. 1995). This is because the Recommended Order prohibits anyone involved in the Track B process on behalf of APS from communicating with or having any contact with employees of an APS affiliate regardless of the nature of such communication or contact. (*See* Recommended Order at 57.) These are yet additional reasons why any further affiliate restrictions beyond those suggested by Staff in the Standards of Conduct should be addressed in the Code of Conduct proceeding discussed in the Recommended Order.

Based on all of the evidence offered during the hearing, Staff concluded that the Standards of Conduct should "strive for separation of information, rather than complete separation of function." (Staff Initial Brief at 8.) That conclusion took into account the

corporate structure created by PWCC in response to prior Commission orders. As the Staff recommendation acknowledges, a corporate structure put in place over a period of three, and in some instances, nearly 20 years without the sort of inter-company restrictions now suggested in this proceeding cannot simply be changed overnight.

Nonetheless, PWCC has already taken significant steps to address each of the concerns set out in the Track A order. PWCC recently moved the PWCC Marketing and Trading group back to APS, which was one of Staff's recommendations in Track A that the Commission did not require. APS also has clearly indicated that the APS Procurement Team will not provide any support to PWEC should that affiliate elect to participate in the solicitation process.[17] To require a complete overhaul of the corporate structure, as the Recommended Order would do, is inherently unreasonable.

Several of the "guidelines" proposed in the Recommended Order raise especially significant and even impossible implementation problems. First, the Recommended Order would preclude any employee involved in the solicitation process for APS from having any contact with any employee "who may be involved in the preparation of a bid in the solicitation process." (Recommended Order at 57, 72 [emphasis added].) Are APS employees who encounter an employee of an affiliate now required to shun that affiliate employee because he or she may be involved on behalf of PWEC in the solicitation process? Would APS employees be precluded from eating lunch or attending meetings with employees from an affiliate even if they do not discuss the solicitation process in any way? Are APS employees precluded from riding in the same elevator as employees from an affiliate? Even more troubling, are the Code of Conduct and Ethics employees that advise APS on affiliate issues prohibited from similarly monitoring and advising PWEC on PWEC's obligations under the Code or Standards of Conduct—virtually guaranteeing

[17] With the movement of marketing and trading to APS, PWCC has only a few existing contracts that it will retain until their term expires and is essentially incapable of participating in Track B or any other new power solicitation except perhaps as a guarantor for PWEC.

confusion and inconsistent application of these affiliate restrictions? While such questions may seem to raise ludicrous issues, the Recommended Order, if taken literally, can be read to preclude critical, yet wholly innocent (from the standpoint of Track B) and even meaningless interactions between employees. APS has repeatedly commented throughout these proceedings on the use of overly-broad language in the Staff Report concerning affiliate relations and based on Staff's testimony at the Track B hearing, appeared to be getting its message through. The Recommended Order is a decided step back to an unworkable set of absolutist prohibitions that cannot be reconciled with the holding company structure PWCC has had in place for nearly 20 years.

Similarly, the Recommended Order would "prohibit personnel who provide advice to APS in the solicitation process from communicating with personnel working for APS' parent or affiliates who may be involved in the preparation of a bid in the solicitation process." (*Id.*) That requirement simply ignores the entire concept of a shared service. Again, if read literally, the requirement would preclude all shared services personnel who provide any advice to APS in the solicitation process from providing any support to an APS affiliate <u>even on matters that have nothing to do with the solicitation process</u> and do not even involve APS. Would an attorney who provides basic contract term or tax advice to the APS solicitation team be thereafter precluded from assisting an APS affiliate in negotiating a contract to procure such basic supplies as paper or pencils or managing its property tax exposure in Nevada? Would environmental, safety and health personnel who provide general advice to the solicitation team on the meaning of information provided in a bid response be precluded from assisting Silverhawk in complying with Nevada's applicable environmental laws, even when this PWEC issue has nothing to do with the solicitation process? Would an accountant who performs basic present value or "mark to market" calculations for APS' use in the Track B solicitation process be precluded forever

from providing any accounting services, even those unrelated to the solicitation process, to an APS affiliate?

As these many questions indicate, the implementation of the above two "guidelines" is not nearly as simple as the Recommended Order believes and is fraught with unintended consequences for both APS and its customers. And, they would completely undercut the entire concept of shared services, which have been previously permitted by the Commission and benefit all of the Pinnacle West affiliates, including APS. If PWCC or PWEC are required to retain outside support in areas now designated as shared services, it will not just be those affiliates that will have to absorb higher costs as is so cavalierly noted in the Recommended Order. (Recommended Order at 58.) APS will also incur significantly greater costs because APS will now pay all of those employees' costs. While a requirement precluding employees (APS or shared services) supporting APS in the Track B solicitation process from providing services related to that process to an affiliate would be reasonable and wholly acceptable to APS, the Recommended Order's proposals go far beyond those of any jurisdiction and are simply unworkable.

Finally, the Recommended Order mandates the following:

> In determining whether an act or communication is appropriate, the APS employee should evaluate whether the act or communication would further the Commission's goal of encouraging the development of a robust wholesale generation market in Arizona.

(Recommended Order at 58, 72.) This requirement is unreasonable on its face. An APS employee's duty is to further the interests of the Company, its customers and its community while complying with the law. No duty should be owed to promote some amorphous "robust wholesale market." The language in the Recommended Order is also so vague that no APS employee would ever be able to apply the requirement in practice. What makes a wholesale market "robust?" What if this "goal" is fundamentally

incompatible with the interests of APS customers?" In Staff's Closing Brief in the Company's pending financing proceeding, Staff makes the following statement under the somber heading "*THE COMMISSION SHOULD NOT SACRIFICE RATEPAYERS' INTERESTS IN ORDER TO PROTECT THE INTERESTS OF THE MERCHANT GENERATORS*":

> Panda urges the Commission to design this transaction based solely upon the goal of protecting the wholesale market. But this is premature: we do not yet know whether there is anything worthwhile to protect. True, the Commission has stated that it favors competition. But the Commission, in its Track A order, has also recognized that the competitive wholesale market is dysfunctional and that FERC has been unable to adequately protect ratepayers.

(Staff Closing Brief in Docket No. E-01345A-02-0707 at 7, [emphasis added].) The Recommended Order should similarly temper its enthusiasm for policies that confuse means with goals and that risk sacrificing both APS customers and the economic health of its electric utilities in the name of competition.

The Recommended Order then goes on to admonish APS that the Commission will "closely scrutiniz[e] the solicitation process for signs of any such abuse." (*Id.*) Particularly dismaying is that the Recommended Order appears to once again presume that APS will act improperly despite no evidence that it has ever done so.

In its proposed amendments, the Company has deleted much of the Recommended Order's discussion on this point. This leaves the issue of affiliate relations to be resolved by the Standards of Conduct as called for in the Staff Report and the Code of Conduct hearing mandated by Decision No. 65154 and further discussed in the Recommended Order. Even if the Commission is unwilling to adopt the Company's language, it is now clear that PWCC is essentially out of the energy business and will certainly not be a bidder in Track B or anything else. Thus references to PWCC in the ALJ's discussion of Standards of Conduct should be deleted. This will avoid some of the bizarre hypothetical situations discussed above.

VI.
CONCLUSION

The Recommended Order simply won't work. It is a recipe for ineffective, costly and intrusive micro-management, with only the magnitude and timing of the negative impact on APS and its customers in question. And its very ambiguity will allow any unsuccessful Track B bidder to claim that one or another of its numerous provisions has been violated or not given sufficient consideration and weight. Attached to these Exceptions are the Company's proposed amendments to the Recommended Order, which largely consist of deleting the more counter-productive, impractical, vague, and ambiguous portions of the discussion, findings and conclusions. Although still far from perfect, this would restore much of Staff's original position in this proceeding as set forth in its October Staff Report, which both APS and TEP found to be, in large part, a workable approach for the initial Track B solicitation.

RESPECTFULLY SUBMITTED this 10th day of February 2003.

SNELL & WILMER L.L.P.

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Original and 21 copies of the foregoing filed this 10th day of February 2003, with:

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Phoenix, AZ 85007

Copies of the foregoing mailed, faxed or transmitted electronically this 10th day of February 2003, to:

All parties of record

Vicki DiCola

Vicki DiCola

Exhibit A

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT NO. 1
TO RECOMMENDED OPINION AND ORDER

(EVALUATION STANDARDS)

TIME/DATE PREPARED: February 10, 2003

COMPANY: Generic Restructuring - Track B AGENDA ITEM NO. U-1

DOCKET NO. E-00000A-02-0051 OPEN MEETING DATE: February 21, 2003

Page 43, Lines 1 to 6½:

DELETE from "In making its determination…" to end of paragraph

Page 44, Lines 6½ to 9:

DELETE from "As to Sempra and SWPG's…" to "…APS' and TEP's actions, we agree."

Page 44, Line 11:

DELETE "while taking environmental concerns into account."

Page 49, Lines 5½ to 12:

DELETE paragraph

INSERT "We agree that the utilities can require such information from prospective bidders. Whether they do so, however, will be at the utilities' discretion."

Page 51, Lines 1 to 6½:

DELETE from "while being mindful…" to end of paragraph

Page 68, Line 19 to 23:

DELETE Finding of Fact 30 from "APS and TEP shall test…" to "…existing assets."

Page 68, Line 26 to Page 69, Line 6:

DELETE Finding of Fact 31

Page 70, Lines 25 to 27:

DELETE "In determining the appropriate resource…" to "…future upswings in power prices."

Page 71, Lines 2 to 9:

DELETE from "including…" to "…conformity with those goals."

Page 75, Lines 3 to 5:

DELETE from "to determine whether reliable…" to "…their own existing assets."

Page 75, Lines 10 to 17:

DELETE Conclusion of Law 9

1307640.1

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT NO. 2
TO RECOMMENDED OPINION AND ORDER

(PROCUREMENT AMOUNT AND PROCESS)

TIME/DATE PREPARED: February 10, 2003

COMPANY: Generic Restructuring - Track B AGENDA ITEM NO. U-1

DOCKET NO. E-00000A-02-0051 OPEN MEETING DATE: February 21, 2003

Page 10, Lines 17 to 26:

DELETE from "Decision No. 65154" to the end of paragraph

Page 14, Line 9 to Page 15, Line 4:

DELETE through "...their own existing assets."

INSERT "Although APS and TEP are correct in their interpretation of the Track A decision, this does not mean they, and perhaps their customers, would not benefit from looking at a broader solicitation that includes forecast estimates of economy energy."

Page 15, Line 6 ½:

DELETE "must"

Page 15, Lines 11 to 26:

DELETE from "and that it not be limited..." to the end of page

Page 16, Lines 15 ½ to 18:

DELETE sentence and citation

Page 18, Line ½:

DELETE Footnote 8

Page 19, Line 24½:

DELETE "necessary"

Page 20, Line ½:

DELETE "whether a utility has an affiliate operating in the Arizona wholesale market or not"

Page 23, Line 2:

INSERT ", in the future," AFTER "may"

Page 23, Line 3:

REPLACE "solicitation" WITH "issue"

Page 23, Lines 5 to 6 ½:

DELETE from "will make…" to "…existing assets,"

INSERT "will be permitted to recover in future rates all fixed costs (including return) of existing utility-owned assets currently in rates,"

Page 23, Line 7 ½:

REPLACE "is within their control" WITH "should be minimal"

Page 23, Line 7 ½ to 11:

DELETE from "The RMR studies…" to end of paragraph

INSERT "We will not require APS to solicit for utility-provided RMR in this first solicitation. Rather, we will ask Staff to organize a set of workshops throughout 2003 to devise, if possible, a specific proposal for soliciting and evaluating long-term RMR options."

Page 23, Lines 12 to 15 ½:

DELETE paragraph

Page 23, Line 20 ½:

REPLACE "the" WITH "a"

Page 23, Line 22 ½ to Page 25, Line 14 ½:

DELETE from "We believe…" to end of section

Page 26, Line 21 ½ to Page 27, Line 13 ½:

DELETE

Page 28, Lines 5 ½ to 14 ½:

DELETE paragraph

INSERT "The Yuma RMR situation is more complicated than either Phoenix or Tucson because the potential market is so much smaller and there is no uncommitted non-APS generation within the constraint. Nevertheless, we believe that long-term options to address RMR requirements in Yuma should be explored in the RMR workshops mandated by this decision."

Page 31, Lines 23 ½ to 25:

REPLACE "fill unplanned or unexpected needs from the spot market" with "procure economy energy"

Page 31, Line 25 to Page 32, Line 5 ½:

DELETE from "However, the record…" to "…for this energy."

INSERT "As discussed previously, we believe a broader solicitation that includes economy energy proposals can provide APS with valuable information at little or no risk, since it can always refuse proposals not in the best interests of APS customers."

Page 32, Line 5 ½:

REPLACE "is necessary so that" WITH "will allow"

Page 32, Line 6 ½:

REPLACE "can" WITH "to"

Page 32, Line 7 ½:

REPLACE "the spot market" WITH "its current practices"

Page 32, Lines 7 ½ to 13 ½:

DELETE from "APS has previously…" to "…program."

Page 32, Lines 13 ½ to 14 ½:

REPLACE "than spot market purchases" WITH ","

Page 32, Lines 14 ½ to 19:

DELETE from "We are requiring…" to end of paragraph

Page 32, Lines 21 ½ to 25:

DELETE from "is not the…" to "…solicitation process."

INSERT "will not be adopted at this time."

Page 32, Line 26

INSERT "economy" AFTER "third-party"

Page 32, Line 27 to Page 33, Line 2:

DELETE from "Such a solicitation…" to end of paragraph

Page 33, Line 10 to Page 34, Line 2:

DELETE paragraph

INSERT "TEP's economy energy purchases are indistinguishable from those of APS. And we will require TEP to secure proposals for economy energy in the same manner as APS and for the same reasons. As in the case of APS, TEP may refuse to accept economy energy offers that it finds are not in the best interests of TEP customers."

Page 34, Lines 19 to 20:

DELETE from "and find it reasonable…" to "…set forth in the Staff Report."

INSERT "except that consistent with our earlier discussion, we will exclude RMR."

Page 34, Line 22½ to Page 35, Line 2:

DELETE "with the addition of the necessary RMR…" to "…set forth in the Staff Report."

INSERT "but without RMR."

Page 35, Lines 11 to 18:

DELETE paragraph

INSERT "We will adopt Staff's estimates with the same exclusion of RMR. As with APS, this exclusion does not mean TEP should not consider proposals from merchant generators and others that may be able to reduce RMR hours in a cost-effective manner."

Page 36, Lines 18-19:

DELETE from "We agree with the statement,…" to "…in Exh. S-1."

Page 36, Lines 24 to 27:

DELETE from "with the addition of the necessary RMR amounts..." to "...the Staff Report."

INSERT "but again without the RMR amounts."

Page 37, Lines 17 to 20:

DELETE from "with the exception of the amounts..." to end of paragraph

INSERT "excepting RMR amounts."

Page 39, Lines 1 to 3:

DELETE from "it appears that..." to end of paragraph

INSERT "the RFP process appears a more practical vehicle for this initial solicitation. This does not mean that auctions have been rejected and may be used in subsequent or secondary solicitations."

Page 43, Line 27:

INSERT new paragraph: "In its Exceptions, APS suggested staggering the bid evaluation. Bids covering only 2003 would be evaluated first in accordance with the schedule set forth in the Staff Report. Multi-year bids or bids for deliveries after 2003 would require additional evaluation and awards would be announced approximately three weeks later."

Page 44, Line 11:

INSERT new sentence: "As to APS' request to stagger the evaluation, this appears reasonable and prudent, and thus will be permitted."

Page 50, Line 22½:

DELETE from "exceeding their requirements..." to "...own existing assets,"

Page 65, Lines 2 to 4:

DELETE from "why future competitive solicitation..." to "...explicit finding here. However,"

INSERT "to make any determination of how future Track B procurements will be conducted at this time."

Page 68, Line 9:

DELETE from "including whether APS and TEP are required to accept any bids;"

Page 68, Lines 13 to 18:

DELETE Findings of Fact 28 and 29

Page 69, Lines 10 to 12:

DELETE from "should increase the benefits…" to "…Arizona's load pocket problems."

INSERT "is not appropriate at this time but will be considered in a series of workshops sponsored by Staff for inclusion in any future Track B solicitations."

Page 69, Lines 13 to 20:

DELETE Findings of Fact 34 to 35

Page 69, Line 24 to Page 70, Line 3:

DELETE Findings of Fact 37 to 39

Page 70, Line 4:

DELETE "at a minimum,"

Page 70, Lines 5 to 8:

DELETE from "with the addition of the necessary RMR…" to "…the Staff Report."

INSERT "as modified herein."

Page 70, Line 9:

DELETE "at a minimum,"

Page 70, Lines 10 to 13:

DELETE from "with the addition of the necessary RMR…" to "…the Staff Report."

INSERT "as modified herein."

Page 70, Line 14:

DELETE "at a minimum,"

Page 70, Lines 15 to 18:

DELETE from "with the addition of the necessary RMR…" to "…the Staff Report."

INSERT "as modified herein."

Page 70, Line 19:

DELETE "at a minimum,"

Page 70, Lines 20 to 23:

DELETE from "with the exception of the amounts labeled…" to "…set forth in the Staff Report."

INSERT "as modified herein."

1307641.1

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT NO. 3
TO RECOMMENDED OPINION AND ORDER

(COMMISSION APPROVAL)

TIME/DATE PREPARED: February 10, 2003

COMPANY: Generic Restructuring - Track B AGENDA ITEM NO. U-1

DOCKET NO. E-00000A-02-0051 OPEN MEETING DATE: February 21, 2003

Page 63, Lines 1 to 2:

DELETE from "We disagree ..." to "...manner by which APS procures power."

Page 63, Lines 6½ to 25:

DELETE from "Secondly, the Track B solicitation..." to "...pose a substantial risk to consumers."

INSERT "That being said, this first Track B solicitation is already facing considerable uncertainty. In an effort to encourage both APS and TEP to accept reasonable proposals from the Track B bidders even though there are many questions about the structure and direction of the wholesale market, both presently and in the future, we will deem as just and reasonable all contracts awarded as a result of the Track B solicitation if the independent monitor determines that such contracts were the result of a fair and open solicitation in conformance with the procedures mandated herein. If the independent monitor is unable to make such a determination, APS and TEP can apply to the Commission for expedited approval of individual agreements for deliveries at the conclusion of each solicitation."

Page 74, Lines 9 to 15:

DELETE Findings of Fact 65 and 66

INSERT new Finding of Fact: "All contracts awarded as a result of the Track B solicitation will be deemed just and reasonable if the independent monitor determines that such contracts were the result of a fair and open solicitation in conformance with the procedures mandated herein. If the independent monitor is unable to make such a determination, APS and TEP can apply to the Commission for approval of individual agreements for deliveries at the conclusion of each solicitation."

Page 75, Lines 24 to 25:

DELETE Conclusion of Law 12

INSERT new Conclusion of Law: "All contracts awarded as a result of each Track B solicitation will be deemed just and reasonable if the independent monitor determines that such contracts were the result of a fair and open solicitation in conformance with the procedures mandated herein. If the independent monitor is unable to make such a determination, APS and TEP can apply to the Commission for approval of individual agreements for deliveries at the conclusion of each solicitation."

1307642.1

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT NO. 4
TO RECOMMENDED OPINION AND ORDER

(STANDARDS OF CONDUCT)

TIME/DATE PREPARED: February 10, 2003

COMPANY: Generic Restructuring - Track B AGENDA ITEM NO. U-1

DOCKET NO. E-00000A-02-0051 OPEN MEETING DATE: February 21, 2003

Page 51, Line 27:

REPLACE "PWEC" WITH "Pinnacle West"

INSERT "Recently, dispatch and other Pinnacle West functions were transferred back to APS. This moots PGR, Reliant and Harquahala's concerns." AFTER "Pinnacle West"

Page 52, Line 23½ to Page 53, Line3

DELETE from "In particular,..." to end of paragraph

Page 55, Line 10:

INSERT new paragraph "Subsequent to the hearing in this matter, Pinnacle West publicly announced that M&T functions were being transferred back to APS. This leaves Pinnacle West with only a few existing wholesale contracts to have administered. It also essentially takes Pinnacle West out of the competitive electric business and returns it to the status of being merely a holding company. This is very significant because it removes most of the concerns about shared services between APS and Pinnacle West. Any relationships between APS and PWEC are best addressed by the Standards of Conduct called for under the Staff Report and the Code of Conduct required by Decision No. 65154."

Page 56, Line 27 to Page 58, Line 2:

DELETE from "However, the content..." to "...at their own expense."

Page 58, Lines 5½ to 6½:

DELETE "along with the additional requirements stated above,"

Page 58, Lines 7½ to 22½:

DELETE from "We believe that a requirement…" to "…abuse."

Page 59, Lines 22½ to 23½:

DELETE "File for Commission approval" and "adopting such a practice."

INSERT "We will require APS to submit a draft protocol to Staff and the Monitor."

Page 71, Lines 21 to 24:

DELETE Finding of Fact 49

INSERT new Finding of Fact: "Subsequent to the hearing, Pinnacle West publicly announced that the energy functions at Pinnacle West affecting APS were being transferred back to APS. Pinnacle West would no longer seek power contracts with APS. This moots our concern over the exchange of information between APS and Pinnacle West. APS relations with PWEC during the Track B solicitation should be addressed by the Standards of Conduct called for by Staff and, more long term, in the Code of Conduct proceeding called for by Decision No. 65154."

Page 71, Lines 25 to 28:

DELETE Finding of Fact 50

Page 72, Lines 1 to 12:

DELETE Findings of Fact 51 to 53

Page 72, Lines 13 to 15:

DELETE sentence beginning with "APS shall adopt …"

Page 72, Lines 15-16

REPLACE "adopting this practice, for Commission approval," WITH "with Staff and the Independent Monitor"

Page 72, Lines 17-25

DELETE Finding of Fact 55

Page 75, Lines 18 to 20:

DELETE Conclusion of Law 10

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT NO. 5
TO RECOMMENDED OPINION AND ORDER

(TYPOGRAPHICAL ERRORS AND MISCELLANEOUS CHANGES)

TIME/DATE PREPARED: February 10, 2003

COMPANY: Generic Restructuring - Track B AGENDA ITEM NO. U-1

DOCKET NO. E-00000A-02-0051 OPEN MEETING DATE: February 21, 2003

Page 8, Line 2:

INSERT, AFTER "November 18, 2002,": "APS, TEP,"

Page 11, Lines 3 to 4:

DELETE "Also pertinent to Track B"

Page 13, Lines 4 to 5:

DELETE "APS identified in its Needs Assessment"

Page 17, Line 1:

REPLACE "portion of the increase" WITH "refinement"

Page 17, Line 2:

REPLACE "addition of" WITH "use of revised"

Page 25, Line 18:

REPLACE "2007" WITH "2005"

Page 67, Line 27:

REPLACE "the parties," WITH "Staff,"

Page 76, Lines 7 to 10:

DELETE from "IT IS FURTHER ORDERED…" to "…prohibit the restraint of trade."[1]

1307644.1

[1] There is no discussion in the order to the intent or meaning of this ordering paragraph, nor to its effect or lack of effect on A.R.S. § 40-286.